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Whither Public Power in Northern California? PG&E's Proposal to Buy SMUD

Assembly Committee on Utilities and Commerce

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Informational Hearing
OF
Assembly Utilities and Commerce Committee

**WHITHER PUBLIC POWER
IN NORTHERN CALIFORNIA?
PG&E'S PROPOSAL TO BUY SMUD**



Museum of Science and Industry
Hearst Theatre
Los Angeles, California
October 6, 1987

CHAIRWOMAN: ASSEMBLYWOMAN GWEN MOORE
William Julian, Committee Consultant
Yvonne Wilson, Committee Secretary

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California Legislature

Assembly Committee

on

Utilities and Commerce

GWEN MOORE

CHAIRWOMAN

MEMBER OF THE ASSEMBLY

FORTY-NINTH DISTRICT

Interim Informational Hearing

Tuesday, October 6, 1987

Room 126, State Capitol Sacramento

**WHETHER PUBLIC POWER IN NORTHERN CALIFORNIA ?
PG & E'S PROPOSAL TO BUY SMUD**

Agenda

I. Opening Remarks: Assemblywoman Gwen Moore

II. Testimony

Howard Golub, General Counsel, Pacific Gas & Electric Company
Cliff Wilcox, Board Chair, Sacramento Municipal Utilities District

Panel on Rancho Seco

PG & E

Joe Firlit, Assistant General Manager, Nuclear Power Production, SMUD
Michael Remy, Sacramentoans for Safe Energy (SAFE)

Nuclear Regulatory Commission

Greg Cook, Senior Public Information Officer
Martin G. Malsch, Deputy General Counsel for Licensing and Regulation

Panel on Resource Options and Transmission Access

PG & E

SMUD

Jerry Jordan, California Municipal Utilities Association
Gordon Hoyt, Past President, American Public Power Association
Dr. Jan Hamrin, Independent Energy Producers Association
David Coleman, Western Area Power Administration (WAPA)
Steve Wright, Bonneville Power Administration (BPA)

Customer Perspectives

Jim Butz, Manager of Electrical Supply, Air Products and Chemical Inc.
Ed Lewis, Sacramento Council of Senior Citizen Organizations
Dennis Diede, SMUD Ratepayers Association

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California Legislature

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WHITHER PUBLIC POWER IN NORTHERN CALIFORNIA: PG & E AND SMUD

INTRODUCTION

On September 3, 1987, Pacific Gas & Electric Company (PG & E) Chairman Richard Clarke proposed that PG & E buy the Sacramento Municipal Utility District, close down its troubled nuclear powerplant Rancho Seco, and consolidate SMUD's electrical operations with PG & E's existing gas supply operation in the Sacramento area. This dramatic proposal, and the issues it raises about SMUD, and energy supply markets in Northern California is the subject matter of this hearing.

SMUD'S PROBLEMS

The Sacramento Municipal Utilities District (SMUD) is the second largest publicly owned electric system in California, and one of the largest in the country. It is at the center of a vibrant group of publicly owned power systems in Northern California. Its health and vitality are intimately connected to future of public power in Northern California.

SMUD is the fifth largest retail electric distribution utility in California. It serves approximately 360,000 residential customers and 40,000 businesses. It obtains power from a combination of its own facilities -- it owns and operates the Upper American River Project (hydro), geothermal properties in Lake County, and Rancho Seco (nuclear) -- and purchases from various state and federal sources, including a large entitlement from the federal Central Valley Project, operated by the Western Area Power Administration (WAPA.)

Since December 1985, SMUD has wrestled with the shutdown of its principal thermal power source, Rancho Seco, a nuclear power plant located 20 miles southeast of Sacramento. Rancho Seco represents approximately 35 % of SMUD's assets, and 40 % of its generation resources (55 % of the resources it owns.) SMUD's rates for electric service have climbed steadily, and the District's financial strength has steadily eroded. At a time when its service area is experiencing explosive growth, SMUD has not been well equipped to meet its needs.

The Rancho Seco outage has resulted in SMUD's operating at a loss for the past two years, despite nearly doubling rates. (Average revenue per residential kwh was 4.23 ¢ for 1984, 6.55 ¢ in the first six months of 1987, a 55 % increase; business revenue went from 3.33 ¢ to 5.31 ¢, a 57 % increase. Rates will go up another 8 % effective October 1.) In recognition of the public's intense interest in the steady escalation in rates, the Legislature last year directed SMUD to expand public notice and develop procedures for expanding public input into the rate setting process. AB 3210 (Moore), ch. 1396 (1986).

The Rancho Seco outage impacts SMUD rates in several ways. It was itself a relatively low-cost source of power for retail sales (although it is now clear that costs were artificially suppressed due to unacceptably low expenditures for operation and maintenance (O & M), capital additions and accruals for decommissioning.) It also provided energy and capacity for resale which supported its contractual obligations to PG & E. (See below, page , for a brief description of pending litigation on this matter.)

Operating at a loss during a period of heavy capital expenditures for Rancho Seco has sapped the District's financial strength. SMUD is very highly leveraged (contains a large proportion of debt in its capitalization), and includes among its assets deferred expenses for power it is currently purchasing that will have to be recovered in future rates. SMUD bonds are now rated at the lowest investment grade. In recognition of the fact of diminished financial capability, the Legislature authorized additional short-term borrowing authority to pay purchased energy costs (SB 107 (L. Greene), ch. ___, (1987)).

The District's current plan calls for the District to restart Rancho Seco in January 1988, with gradual escalation to full power operation scheduled for June 1988. SMUD is spending \$20 million a month in pursuit of this objective. There are a number of obstacles to restart, the most important being NRC approval of hardware modifications, sytem upgrading, improved managerial processes and operator training. Widespread public misgivings about restart is reflected in a ballot initiative intended to

force permanent closure of the plant irrespective of restart. An analysis by SMUD of the effects of termination before restart prepared for its most recent bond Prospectus (pp. 19-22) indicates that closure would eliminate existing customer equity and raise average costs to 7.51 ¢ in 1988, and 10.2 ¢ in 1991. The assumptions about levels of replacement power requirements and replacement power costs are not clearly stated in the study.

Financial and operational turmoil has been accompanied by instability at top management levels. SMUD has changed general managers three times in the past three years, and currently has no permanent general manager. Operational responsibility for Rancho Seco and the restart program has been drastically restructured twice in the past two years. The current arrangement calls for complete managerial independence for the nuclear restart and operations component of the SMUD organization, in effect parallel organizations for the nuclear and non-nuclear elements.

SMUD'S RESPONSE TO ITS PROBLEMS

SMUD has not developed a clear-cut strategic plan for dealing with its problems. Until recently its efforts have been principally directed toward restart of Rancho Seco, and improvising operational approaches and the rates required to fund them while restart continues. As the restart process has lengthened due to unanticipated problems and a widening scope of concerns on the part of the Nuclear Regulatory Commission (NRC), this improvisational approach has appeared too limited, and the board has begun to pursue two new directions, risk-sharing for Rancho Seco and exploration of competitive options for electric generation.

A) Risk Sharing

The Board began to explore measures for sharing the risk of ownership of Rancho Seco in the spring of 1987, and employed a consulting firm to explore these approaches (Palmer-Bellevue.) Risk-sharing options identified at the September 17, 1987 board meeting include

- ° divestment (sale) of Rancho Seco, probably through a phased purchase by an entity which would initially be a contract operator of the plant.
- ° divestment (sale) of all of SMUD's generating resources, including its hydro system and geothermal facilities as well as Rancho Seco, to a joint venture (partnership) including other western states utilities and investment bankers.

- ° Repowering Rancho Seco with a non-nuclear power source, presumably natural gas, in a joint venture including El Paso Natural Gas and a firm or firms specializing in co-generation technology.
- ° Immediate shutdown
- ° Sale of the system to PG & E

Any of the options which leave the facility license with SMUD would carry with it the obligation to decommission the plant. Decommissioning is estimated in SMUD's current budget to cost \$122 in 1987 dollars; in SMUD's Rancho Seco shutdown analysis to cost \$200 million; in PG & E's estimation \$230 to 280 million. The cost of decommissioning escalates with increasing plant investment and use. SMUD has set aside \$38.5 million toward this obligation.

B) Expanding Power Purchases

At a meeting of the Board of Directors in July, the SMUD Board called for the SMUD management to begin to solicit offers for electric power resources to meet the District's long-term future needs, while emphasizing that the request for proposals did not reflect a lessened commitment to the restart program at Rancho Seco. The solicitation elicited a number of proposals, including one from the federal Bonneville Power Administration to sell up to 1350 megawatts of power with energy delivered a price at or below 4 ¢, and one from PG & E for up to 1000 megawatts.

The most dramatic being the September 3 offer by the Pacific Gas & Electric Company (PG & E) to buy the district.

The proposals include offers aggregating 5000 megawatts of capacity, three times the District's needs. It is important to emphasize that most of the proposals require delivery of the electricity to SMUD, over transmission lines owned by PG & E. (See below, page .)

The terms of the PG & E offer included

- ° assumption of all SMUD outstanding debts.
- ° permanent shutdown of Rancho Seco, and assumption of the decommissioning obligation. PG & E estimates the cost at \$230 to \$280 million in current dollars.
- ° a guarantee of employment for current SMUD employees.

° a rate freeze of indefinite duration.

The details of the proposal will be fleshed out somewhat by Chairman of the Board Richard Clarke at the SMUD board meeting on Thursday evening, October 1.

SMUD propounded a list of questions to PG & E concerning the proposal on Wednesday, September 30, which are included in the information packet.

PACIFIC GAS & ELECTRIC COMPANY AND ITS MARKETS

PG & E is the largest privately owned energy utility in the world. Its combined electric and gas revenues totalled \$12 billion in 1986.

PG & E provides retail electric and gas service in Northern California, to approximately 3.5 million households, and 400,000 businesses. This is provided on a monopoly basis through its retail distribution facilities. PG & E strives for complete vertical integration -- it strives for monopoly at the production, transmission and distribution levels -- although its legal monopoly extends only to retail markets. That monopoly is being eroded in both electricity and gas service for business customers.

As a combination (electric and gas) utility, it heavily influences the intensity of intermodal competition (gas versus electric) for retail energy use in the areas where it provides both services. In an area like Sacramento, PG & E gas service competes with SMUD electric service for certain energy applications, particularly heating and various industrial applications. In other areas, where it provides both services at retail, PG & E competes for electricity sales to other distributors (munis, public districts and other utilities) from its production facilities (powerplants) with private energy producers, publicly owned energy producers, and imports from outside its service area, particularly the Pacific Northwest.

PG & E's retail rates and terms of service are set by the Public Utilities Commission. The PUC has been in the process of restructuring both electric and gas regulation to enable PG & E to preserve its market share against actual and potential competitors. PG & E's cost of service has historically been substantially higher than SMUD's. Comparative rates have reflected this difference (PG & E has been 30 to 50 percent higher), although the gap has narrowed substantially in recent years.

Like SMUD, PG & E's investment in generation resources is heavily concentrated in a single nuclear facility. Diablo Canyon represents about 30 % of PG & E total assets, although only 12 % of its electrical capacity. PG & E rates do not currently reflect the full ownership costs of Diablo Canyon, although the PUC staff contends that current PG & E rates are at an appropriate level to recover the reasonable and prudent ownership costs. PG & E wants a substantial electric rate increase (as much as 15 %) for Diablo Canyon.

PG & E also owns and operates the Northern California transmission system, which moves electricity among a variety of public and private power producers and consumers, including the federal Central Valley Project, the State Department of Water Resources, nineteen municipally owned power systems, and a number of water districts, irrigation districts, public utility districts and municipal utility districts. An administrative law judge at the Federal Energy Regulatory Commission (FERC) ruled in 1983 that the transmission system is a bottleneck facility under the federal anti-trust laws, and that PG & E would have to renegotiate the contracts providing transmission service to facilitate access for other producers, and to enhance competition. This process is continuing, although very slowly.

PG & E and SMUD

SMUD and PG & E have a long and colorful history.

SMUD began operations in 1947 when, after nearly twenty-five years of litigation and public controversy, it took possession of PG & E's properties in the Sacramento area and began selling retail electric service. One of PG & E's stated objectives in the SMUD buyout proposal is reclaiming its lost monopoly in the Sacramento area.

PG & E has a comprehensive agreement with SMUD, whereby SMUD operations are integrated into the PG & E system, and SMUD and PG & E sell to each other and exchange with each other energy and capacity from their respective systems. SMUD has not delivered energy or capacity to PG & E from Rancho Seco for almost two years. PG & E contends that under the agreement it is not obligated to make capacity payments for the non-operating facility; it has refused to do so. SMUD contends that so long as it acts with due diligence to restore Rancho Seco to operation, it is entitled to capacity payments. SMUD has been purchasing large quantities of replacement power from PG & E, and withholding payment offsetting amounts claimed) to reflect its entitlement to capacity payments. The controversy is before the Federal Energy Regulatory Commission, which is attempting to facilitate a settlement.

SMUD and its sister public power agencies have engaged in a lively set of battles with PG & E over the years. In addition to the federal anti-trust litigation described briefly above, SMUD actively sought to succeed to PG & E's federal licenses for hydroelectric production on California rivers as they expired in the late 1970's and 1980's. (Such licenses, many granted in the 1920's, are generally for a fifty year term, and authorize construction and operation of hydroelectric facilities on California rivers. Until amended in 1985, federal law provided a preference for public entities as licensees.)

QUESTIONS OF INTEREST TO THE COMMITTEE

THE CURRENT SITUATION

- 1) Describe the current PG & E/SMUD integration agreement, and the basic obligations of each under that agreement.
- 2) Describe the status of the litigation under that agreement, including claims of the respective parties for breach of the agreement.
- 3) Describe the status of negotiations for transmission access (wheeling) for SMUD to third party power suppliers (GPPL, FERC Docket U-7777, COT, etc.)
- 4) Describe the current status of proposals by PG & E, and by third parties to furnish electrical energy and capacity to SMUD.
- 5) Describe the current financial and operating condition of the respective parties (PG & E and SMUD) along with any contingencies.
- 6) Describe SMUD's procedures for setting rates and policies with respect to rates.

RANCHO SECO

- 1) What is the current status of the restart effort. Specifically, with respect to:
 - ° Fulfilling NRC license commitments
 - ° Repair of hardware and facilities

- ° Construction activities
 - ° Expenditures to date and additional committed resources
 - ° the prospects for full-power operation
- 2) What are the forecasted costs of Rancho Seco capacity and energy if restart is accomplished ?
 - 3) What are the alternatives to operation of the nuclear system at Rancho Seco ?
 - 4) Why does PG & E believe that a shut-down is appropriate ?
 - 5) What are the costs of a shut-down
 - ° for PG & E ?
 - ° for SMUD ?
 - 6) What are the costs of decommissioning, and the respective options for defraying those costs ?

THE PROPOSED ACQUISITION

- 1) What procedures are contemplated for negotiating on the acquisition proposal ?
- 2) What is the role of the Public Utilities Commission in approving any acquisition, or disposition of acquired assets, by PG & E ?

Specifically, with respect to

- ° the reasonableness of the purchase price
 - ° goodwill, intangibles or going concern value
 - ° a retail rate differential, or rate freeze
 - ° write-off of Rancho Seco
 - ° decommissioning of Rancho Seco
- 3) What is the role of the customer-members of SMUD in approving any sale or disposition of assets by SMUD ?

ASSEMBLY COMMITTEE
ON
UTILITIES AND COMMERCE
Gwen Moore, Chairwoman

WHITHER PUBLIC POWER IN NORTHERN CALIFORNIA?
PG&E's PROPOSAL TO BUY SMUD

State Capitol, Room 126
Sacramento, California
October 6, 1987

CHAIRWOMAN GWEN MOORE: PG&E's offer to buy SMUD is potentially a watershed in the history of energy supply in Northern California. Northern California demonstrates a great variety in the types of public and private entities that provide water and power to our citizens. SMUD is the largest publicly-owned utility in Northern California, and is the key of maintaining that diversity.

I believe that the diversity and the healthy competition that it sustains are extremely valuable. This is "Public Power Week," a fitting time to explore a set of circumstances which have the potential for fundamentally altering the relationship between public and private power companies in California.

There are a number of the pragmatic reasons why the proposal appears quite attractive. Appearances can be deceiving, however. Both SMUD and PG&E are to be commended for beginning a prudent and dignified process for exploring the issues. This hearing will, I hope, contribute to the process of clarifying the options available to SMUD and its customer owners, and will enable the state legislature to exert its influence where it will have maximum effect for the long-term public good.

It is apparent that the lengthy Rancho Seco outage has negated some of the economic advantages that SMUD enjoys as a utility -- the low interest rates; populous, dense and growing service areas; the access to low-cost hydroelectricity and federally subsidized power. SMUD rates have been climbing steadily at the time when rates for all other electric utilities in California have been stable or declining, and all other energy prices have been falling. The prolonged stress caused by these developments has sapped SMUD's institutional strength and credibility, as well as its finances.

This trend can be reversed, if Rancho Seco is restarted and operates reliably for a period of several years. However, restart is extremely uncertain, putting to one side the pending ballot measure on permanent closure, and the generic concerns with nuclear reactors of the type installed at Rancho Seco. We will hear from the Nuclear Regulatory Commission about what SMUD must do to comply with its license commitments to restart the Ranch. We will also hear from opponents who contend for an immediate shutdown.

PG&E has the size and financial ability to withstand a substantial write-off that closure of Rancho Seco would represent. Sheer bigness may be a consideration here, notwithstanding PG&E's record with Helms Creek and Diablo Canyon.

PG&E is a critical player in a number of issues vital to SMUD. The timing of Rancho Seco closure is intimately bound up

with PG&E's lawsuit over failure to deliver capacity and energy from the Ranch. PG&E controls the transmission access to SMUD over which the substantial offers of new low-cost power would be transmitted. PG&E's actions in this regard may be prudent from the standpoint of PG&E and its customers. Whether it is in the best interest of the state as a whole is another matter, which we hope to explore.

Finally, the customers have been heard through news reports and polls. We will hear publicly from customer representatives who have been involved for some time with these issues.

Our first witness this morning will be Howard Golub, the General Counsel from PG&E, and instead of Cliff Wilcox, we will have John Kehoe from the SMUD board. So, if you two would come forward at this time, we will hear your opening statements.

MR. HOWARD GOLUB: Thank you for the invitation to speak on this important subject.

CHAIRWOMAN MOORE: Let me introduce the members we have with us. We have Richard Polanco from Los Angeles area who has considerable interest in this area. Nolan Frizzelle from the Orange County portion of the state.

MR. GOLUB: As you have observed on September 3, Mr. Clark, our Chief Executive Officer, sent a letter to SMUD in response to a request from SMUD for proposals concerning the ownership of the Rancho Seco Nuclear Power Plant. SMUD had put

out a formal written request for proposals dealing with that situation. It stated in that request for proposal as follows: SMUD will entertain alternative proposals and will consider such proposals in a timely fashion. I might add in addition we were contacted by a consultant for SMUD who encouraged us to make far-reaching and nontraditional proposals part of our review.

In response to that invitation, the letter of September 3rd went out. Our analysis indicated that the many issues facing SMUD did require an innovative and comprehensive solution, which was best achieved by a consolidation of SMUD's electric operations with PG&E's gas operations in the Sacramento area. Our analysis indicated a consolidation of the PG&E and SMUD systems will result in major advantages to both the customers of PG&E and the customers of SMUD.

Now, SMUD faces a number of critical issues. And, let me briefly list them, because I think our offer would be more comprehensible with an understanding of the background. They have these situations they have to face. They have rapidly rising customer rates. I believe in the last two years or so there has been a 84% increase in their rates. They are facing the very substantial cost of restarting Rancho Seco. They are facing specifically financial and regulatory uncertainty at Rancho Seco. I want to emphasize on that point it's not just my conclusion, their own perspective to the financial community indicates that as well. They are faced with reduced credit

rating. Currently their credit rating, I believe, is at the bottom of the spectrum that would still permit investment grade purchases. They have had an unusually high turnover in their senior management. They have a major contractual liability to PG&E to purchase power and capacity under our existing contract. They have a need for future resources to serve the longer-term electric energy needs of the people in the Sacramento area.

When we reviewed the matter and laid out these issues and thought what they were, we realized we are the ideal partner to resolve these difficulties. PG&E has a large and diverse resource mix which is capable reliably meeting electric energy needs of the Sacramento area today and well into the future without the need for major resource additions. We have that capability right now. PG&E is an experienced and substantial electric utility with permanent commitment to the northern/central California area, its people and its economy. We have been in Sacramento for a long time. In fact, we originally brought electricity to the Sacramento area. We have a real commitment to this area. We have the equipment. We have the experience, and we have a dedicated workforce located both within the SMUD area and adjacent to the SMUD area. These resources give us the capability of meeting the needs of the customers in the area.

We have the financial resources to raise the capital needed to serve the customers of the SMUD area. We have a

sophisticated resource planning and power acquisition program to purchase the lowest cost power when available on the open market, and a centralized power dispatch system that through an elaborate computer program dispatches the most economic unit available in the area. We can always use whichever unit results in the least costs to the system.

Now given these basic facts, we submitted a proposal for consolidation which we wanted SMUD to consider. It does emphasize that we do not propose an involuntary consolidation. Our proposal assumes concurrence by the people of the Sacramento area. If that concurrence is not obtained, there will not be a consolidation. That's a real fundamental point here.

Now I know that on September 16 the Sacramento Bee reported that 53% of the people living in the Sacramento area favored accepting the PG&E proposal, only 20% opposed. In other words of those people who had an opinion on the matter, over 2 to 1 were in favor of accepting the PG&E proposal. This is, of course, a poll not a vote of the people.

CHAIRWOMAN MOORE: Who did the polling?

MR. GOLUB: The Sacramento Bee. It's dated September 16. I have a copy with me. I have no expertise other than the fact I read the article of which I'll give you.

But, I think the real point there that there is significant interest in the community. We're working on the premise that there needs to be a concurrence of the people of the community.

CHAIRWOMAN MOORE: One of the beauties of a public power system is the fact that it is citizen-customer owned, and therefore would take their approval. But, of course, if they gave that approval it would be the last time they would have that kind of control over what's happening.

MR. GOLUB: I probably shouldn't endeavor to disagree with you, but I would take a look at that issue. Actually that's not quite correct, because in any area that we serve, the people of the community always have the ability to municipalize the area if they think it is in their best interest. That's the truth from time to time. The people always reserve the right to make the erection from an investor-owned service to...

CHAIRWOMAN MOORE: Let's put it another way so you don't have to disagree with me so we can be accurate. When was the last time that occurred?

MR. GOLUB: There has been ballot measures that were defeated on the merits. I think we have a good program.

CHAIRWOMAN MOORE: So, there's never been an instance when that occurred?

MR. GOLUB: No.

CHAIRWOMAN MOORE: Let me take a moment and introduce a couple of members who have joined us. We have Assemblyman Richard Longshore, Vice Chairman Cathie Wright and we have been joined by Lloyd Connelly who represents the area.

MR. GOLUB: Perhaps I should reintroduce myself. I'm Howard Golub, and I'm General Counsel for Pacific Gas & Electric Company.

Our proposal is premised on the understanding that the people will have to concur in it if it is to go forward. We have presented it in that spirit. Now, the written proposals are variable, but the key points in the proposals -- so you really understand what we are suggesting -- we would purchase all of SMUD's facilities. The restart program at Rancho Seco would be terminated and the plant would be closed permanently. PG&E would assume the very large cost of decommissioning the plant and all the tangible difficulties of decommissioning. I might say the decommissioning costs are estimated between \$1.5 billion and \$2 billion. PG&E would freeze electric rates in the area for several years. That's the rates to the consumers. We would assure SMUD employees job security so that they wouldn't adversely affected by this. We also would take in account the pending lawsuit existing where PG&E is suing SMUD for services we rendered and we wish to be paid for, and we would take that into account, and would not end up being an additional cost to the SMUD ratepayers as may well be the case in the event the litigation goes all the way to conclusion and we would recover a large sum of money. So, that would be another element we would take off the SMUD consumer.

CHAIRWOMAN MOORE: You are giving me a list of advantages to the SMUD customer in having this consolidation take place. So that we are clear on what you perceived the advantages to be let's sort of keep of checklist running. First, you're saying...

MR. GOLUB: We would purchase the facilities. I wasn't arguing it was all benefits. I was just trying to describe it. The first is we would purchase all of their facilities. An evaluation would have to be, obviously, arrived at that was agreeable to both parties. Secondly, we would terminate the restart program at Rancho Seco and we would close the plant permanently. Third, PG&E would assume the costs and the difficulties of decommissioning the plant. I should explain that's a cost and a difficulty that has to be borne either by SMUD if restart the plant or not, because that's part of the process of lifecycle of the nuclear powerplant. We would assume that. Fourth, we would freeze electric rates in the area for several years.

CHAIRWOMAN MOORE: Let's kind of stick with your assuming the costs. Tell me what that means?

MR. GOLUB: Well, the primarily representatives in the Nuclear Regulatory Commission could probably give you a more technical and precise answer, but basically, you have to deal with the fact that you have a plant that has been using radioactive materials. You have to dispose of those materials in

a safe way. The Nuclear Regulatory Commission has its own regulations as to how that is to be done. It involves a lot of safeguards and a lot of expense.

CHAIRWOMAN MOORE: You gave me a \$1.5 billion figure.

MR. GOLUB: \$1.5 to \$2 billion.

CHAIRWOMAN MOORE: All right. That's the projection. That's over the years kind of projection. In today's dollars, give me those figures?

MR. GOLUB: In today's dollars, I would say it is approximately \$250 million present value. If you prefer a range, I'd say between \$250 to \$280 million present dollars. If you put the dollars on the table today.

CHAIRWOMAN MOORE: Mr. Frizzelle.

ASSEMBLYMAN NOLAN FRIZZELLE: We jumped right over the potential value or lack of value of the nuclear power facility. We're going on the assumption that you don't think it's of any particular value currently, liability or an asset? The only advantage it has been in the past is the ratepayers have paid a substantially less for their power while it was operating than most other places in Northern California?

MR. GOLUB: The economics of a nuclear powerplant are heavily driven by its availability. If it is operating all the time it can be very helpful.

ASSEMBLYMAN FRIZZELLE: That's not what I was getting to as far as the question is concerned. Whether or not that

facility, in your opinion, is not worth the money to put it shape to operate?

MR. GOLUB: We looked precisely at that question in our analysis. Our conclusion was that from PG&E's economic perspective and the perspective of what we can do, it did not make sense to continue the restart effort or to keep that plant in operation.

ASSEMBLYMAN FRIZZELLE: I want to stop you there because of the fact the PUC is going to make some decision regarding the rates. You say that you are going to hold your rates to a certain level for a certain period of time even though the PUC essentially establishes what appropriate and what's not appropriate? If the nuclear facility were brought on line at whatever cost that may be and could be operated on basis of some effectiveness or efficiency such that the potential for nuclear generation (which is far greater than any other source as far as the per-unit cost of furnishing the power), is the rate that PUC would approve, not including operating the nuclear facility, less or more than what it would be using standard means of generating power?

MR. GOLUB: You're speaking as to this plant now? Not comparing all nuclear plants?

ASSEMBLYMAN FRIZZELLE: Yes, and what it would cost to repair it and put it on line with your great management abilities?

MR. GOLUB: I thank you for that confidence. But we looked at precisely at the question you're asking, and we estimated that it would far more expensive to restart Rancho Seco and continue to operate it than it is to use other resources that are available to us. Our system average cost and our system incremental cost are far less than the cost of restarting that plant and keeping it going. That's precisely why we engaged it ourselves. We looked at it. We said it is cheaper to use these other resources available to us than to continue to pursue efforts here.

ASSEMBLYMAN FRIZZELLE: Once you got the thing repaired, once it was on line, once you put adequate management capabilities into it over a pay-out period of ten years or fifteen years, would that still be the case?

MR. GOLUB: We do our analysis on a 20 year levelized basis as we call it. We do exactly that.

CHAIRWOMAN MOORE: Let me interrupt for a second. Mr. Frizzelle as we go along we are going to hear from both sides. The considerations that SMUD considers are different than those of PG&E. So, they are coming from two different points for view. Maybe you ought to talk a little bit about some of those points about your write-off, and some of the tax benefits that you get when you do it, and the liabilities, and some of the other kinds things that would be a part of it, so you would get a clear picture of what the differences are

Also, we have been joined by Senator Leroy Greene and Senator John Garamendi, both from this area.

MR. GOLUB: I'll introduce myself again. I'm Howard Golub. I'm general counsel from PG&E.

CHAIRWOMAN MOORE: Mrs. Wright.

MR. GOLUB: The perspectives of PG&E and SMUD effects what's going on here. We looked to whatever resources which are available to us. We have cheaper resources than the projected cost of Rancho Seco over a long period of time. Now, if SMUD were continue to operate as an independent system, they would have to look at their alternative to see whether Rancho Seco is cheaper than their alternatives. But I can tell you we have the cheaper alternative than Rancho Seco. That's why in our proposal we proposed to terminate the restart program and to close the plant. There are more economic sources. Our incremental cost of power, so the extra cost to us today for producing power is about 2½¢. I will leave it to SMUD to give their calculations of what they think it would cost. We have our own calculations. But I think I can tell you pretty much anyone's calculations would be significantly in excess of that.

CHAIRWOMAN MOORE: Those sources then, you don't make them available to SMUD at that cost. Mr. Connelly has a question for you too.

ASSEMBLYWOMAN CATHIE WRIGHT: I pick up on your point where you said PG&E will assume the cost whether you close Rancho

Seco or continue Rancho Seco. Who is going to bear that cost? Is it going to be all the ratepayers in the PG&E area? You said you are going to freeze the rates as far as SMUD is concerned or is it going to be the stockholders? Who is going to absorb that cost?

MR. GOLUB: We're talking about the decommissioning costs? Those costs will be part of the overall package that we will have to deal with. The first point you have to figure out what else you're paying for, what you're giving up and what you're getting to see some of the net economic impact. When all of that is said and done -- and it is very important and complex -- the Public Utilities Commission will determine what portion of the net price -- if I can use that phrase -- we paid is properly included in our ratebase to be ultimately charged back to our customers over a long period of years. I assure you based on personal experience in the hearing room that if we have paid too much, the Public Utilities Commission wouldn't permit us to include it in the ratebase. That fundamentally is the process. The regulatory oversight is in the Public Utilities Commission.

CHAIRWOMAN WRIGHT: So there is a possibility that some ratepayers outside of the SMUD area would pay for this?

MR. GOLUB: Not if we paid too much. If the system works as it suppose to, we wouldn't pay too much. But if we paid too much, that would be a cost borne by our shareholders, not by our customers.

ASSEMBLYWOMAN RICHARD LONGSHORE: Your alternatives on costs, as far as deciding to close Rancho Seco is concerned, what elements went into the figuring the cost of reopening Rancho Seco?

MR. GOLUB: We had several things. We have some estimates that the SMUD people have done of which we did some analysis. We also put our own view on what we thought it would be and developed that. There is a lot of judgment there.

ASSEMBLYMAN LONGSHORE: Any specific elements of cost which pushed it over?

MR. GOLUB: Well, sort of an aggregation. One big cost is the restart cost which need not be incurred at all if the decision is made not to proceed. That's money that hasn't yet been spent that could just be saved for everyone involved. In addition, you have to look to their operating and maintenance costs and we did not in that analysis even include the decommissioning costs, which are enormous. We just made our analysis of their operations.

ASSEMBLYMAN LONGSHORE: I'm not sure that you answered my question?

MR. GOLUB: Let me try again. There are many elements. We sat down, our technical people sat down and said how much would it really cost to get Rancho Seco back online and operate it for a period of basically over 20 years, I think, what they used. There are many elements that go into that. One is what's

the cost of restart? How much does it cost to operate that particular plant? You have to make assumptions about the availability of the plant. Will it be available a lot of the time or a small amount of time. That effects the economics very severely. What would it cost to have backup for that plant? That's another important issue. Any major powerplant of any utility has to have a backup, in case that plant is out for some reason. You have to purchase that service if you don't have it in your own system. When SMUD chose to build Rancho Seco, it chose a strategy of building a very large plant for a system of that size. It's a relatively good size. That plant is very, very large. That means they have to find a source of backup in the event that plant is out. So, that's a cost.

ASSEMBLYMAN LONGSHORE: Obviously, you have the backup. You said you have alternatives.

MR. GOLUB: Of course, PG&E has the backup system, but SMUD doesn't. If you trying to figure out how much SMUD would have to pay in the next 20 years to operate the plant, you are taking into account they have to obtain backup either from PG&E or some other utility, and have to pay some reasonable amount. All of these elements were factored in to figuring out what it would cost to operate the plant. What was not in there was any notion of some write-offs. We're just doing an engineering analysis of how much it costs to get this powerplant restarted and operating compared to other powerplants. It's that kind of

an analysis. I don't have a lot of the details with me. We can provide it.

CHAIRWOMAN MOORE: Mr. Connelly.

ASSEMBLYMAN LLOYD CONNELLY: Mr. Golub, first I want to make an observation. I guess everyone knows this. As I understand the law, the State Legislature would not have to necessarily change the law in order to allow this acquisition of assets to occur. I think Ms. Moore was extremely wise in calling this hearing, because it may well be an example of what's happening here to justify some change in law either with regard to criteria for change or transfer or just something else. As I understand it, nothing we have to say about it today specifically stops you.

I wanted to focus on the engineering study.

CHAIRWOMAN MOORE: There could be, Mr. Connelly. Maybe I should take you through some of the things.

ASSEMBLYMAN CONNELLY: Maybe you should do that. I just had a brief chat with the consultant on that. I don't pretend to be an expert. Could you enlighten me just a little bit? You're getting electricity at 2½¢ per kilowatt. Is that what you do now?

MR. GOLUB: That's our incremental cost. The next kilowatt hour.

ASSEMBLYMAN CONNELLY: Right. Does that include Diablo?

MR. GOLUB: The incremental cost...

ASSEMBLYMAN CONNELLY: I understand the figure at Diablo is like 12½¢. Am I wrong? I may very well be.

MR. GOLUB: The data you've given is incorrect, and I'll give you that number. There are several numbers you can look at to compare with Rancho Seco. Incremental costs I would suggest is probably the most relevant one. What is our extra costs of getting the next kilowatt hour to deliver to the customer? That's 2½¢. Our system average cost, if you took all of our operating facilities and average all the costs together, that's about 5.4¢.

ASSEMBLYMAN CONNELLY: Does that include Diablo?

MR. GOLUB: That includes -- yes. That includes the Diablo cost. I was looking at the footnote here to check that. Diablo itself has its own costs. If you isolate a given plant you're not averaging. That's not a whole lot above our system average actually.

ASSEMBLYMAN CONNELLY: You did an engineering analysis of Rancho Seco based on start-up and likely running pattern and so forth. What was your kilowatt cost there?

MR. GOLUB: I have to emphasize what we did was a preliminary study from the outside. What we were hoping to do is to start a process so we can get at real hard numbers. But, to give you an order of magnitude, I hesitate to be too firm. I would you are probably looking at about 7¢.

ASSEMBLYMAN CONNELLY: Is that an engineering study? I notice your advocate is here. I got the 12½¢ figure from him. What is that figure? Do you recall? My recollection is that the figure with Diablo is substantially higher than 5½.

CHAIRWOMAN MOORE: Mr. Connelly, that sounds like the Diablo figure not being averaged. What he's done here, the figure that you're getting is one averaging all their sources which may be some hydroelectric plants, which are no costs and some of the others. But strictly just Diablo would be the 12¢.

MR. GOLUB: I'd like to check, because my numbers are a lot lower than that. Although we are not proposing to sell....

ASSEMBLYMAN CONNELLY: Excuse me. That a fairly substantiative issue to me, at least from my perspective. I thought the system average figure including Diablo was 12½¢. Did I misunderstand you?

MR. GOLUB: I think there was a misunderstanding. I will recheck the figure.

ASSEMBLYMAN CONNELLY: My understanding if you're just talking exclusively about the cost of electricity produced by Diablo that it is in the neighborhood of 12¢. System-wide average including Diablo is in the rate of 5¢? Got it. In the engineering analysis, I understand, it was preliminary and all the usual cautionary words -- 7¢ for Rancho Seco or in that range.

MR. GOLUB: Roughly.

ASSEMBLYMAN CONNELLY: Have you made that available to SMUD?

MR. GOLUB: No. I don't think it has been asked for. What we want to do very much...

ASSEMBLYMAN CONNELLY: Could I ask you to make that available to SMUD and the Sacramento community so that we could evaluate and compare, because our figure is substantially lower. Then we would have the opportunity to look at it -- you say it is 7¢ and we say it is 4¢ and compare that difference. Because that is very crucial, quite candidly in terms of our decision for other options as well. It seems to me the Board -- and I would like as a citizen to know why there is almost a 75% variation in your projection of cost per kilowatt with Rancho Seco versus our projections. We're making some pretty important decisions, one of which is spending \$20 million a month to crank that puppy up based on an assumption that it operates at 4¢ a kilowatt. Can I just ask that you make that engineering report available to us?

MR. GOLUB: Well the report was very preliminary. I think we could make the information available, leave with the relevant people and provide the basic information. I hesitate because, as you heard me saying, it really isn't a kind of formal study that you want to sit there and argue about it. We basically concluded that our cost was so much below theirs, we didn't have to get into fine points. Once we knew that our incremental cost is 2½¢, that's what we're really comparing.

What's the cost to us of our next resource compared to the cost of operating this plant? If you assume 5¢ for Rancho Seco, it still twice our incremental. I understand what you wanted, but I'm just suggesting we did it in a rough way. We never tried to publicize it or make an issue of it.

ASSEMBLYMAN CONNELLY: I just want to nail you down on this a little bit. This in some respect silhouettes the issue between private and public. The public would make a freedom of information demand if they start being hesitant and we get the report. If it is private, we have to beg a little bit from you. I'm willing to do that because I think that report is that important. Would you actually give the document that your engineers prepared so that our folks can look it and we can look at it as well to see why you came up with 7¢ versus our 4¢?

MR. GOLUB: Mr. Connelly, we have been trying to engage the District in a meaningful dialogue on a series of numbers. Mr. Clark went before the board on October 1 -- I don't think you're begging and I don't think he begged for it -- urged that dialogue be commenced immediately. We would like to do that. I would like to do that as part of a board dialogue. I would hope it would be that. We will be available to meet with whoever who wants to come down. The thing I want to emphasize, though, we didn't want to attack the economic studies done by SMUD on this particular matter, because from our perspective, it is not what we are involved in. We were simply trying to analyze the best alternatives.

ASSEMBLYMAN CONNELLY: I think SMUD ought to look at your proposal with a tough eye, and consider which is the best one to go with. I'm saying right now we're going to be selling \$130 million of bonds in the next week, a good portion of which is go toward the \$20 million a month to put Rancho Seco back online, and if you have a preliminary report that says it is 7¢ a kilowatt instead of 4¢ a kilowatt, John ought to look at that. He ought to ask his people some questions as to why there's a difference. It may well be your work was done hastily or whatever. But we're making decisions right now that are costing millions of dollars, or SMUD is, on an assumption that it is 4¢. It sets a variation there. It is a big one. If you can make that available to us, that would help us not only in terms of ultimately evaluating your proposal, but also helping us in the decisions we're making quite candidly in the next 30 to 90 days.

MR. GOLUB: Yes, I would like that to be a mutual exchange of information. If we could do that, I would like to. As long as we can both get into it and have an honest exchange of data, we would like to.

CHAIRWOMAN MOORE: Before we get into that, I think that's important, but I think we're comparing apples with oranges and a few other things. I want to go back to where we started in trying to get some understanding of the economics. There is a difference in perceptions. I haven't heard the 4¢ figure for a long time, and I don't know where that came from unless it is

based on some assumptions that are not really there. So when SMUD gets its opportunity to make its presentation, we can go into that. We have a long hearing. I want to caution members we don't want to spend too much time, so we don't miss hearing from everyone.

Could you kindly go back, you have been tying down the economics, to where you are with respect to write-offs and some of the other kinds of things.

MR. GOLUB: This economic analysis looks on the real economics of the plant. Write-offs have not been part of the analysis.

CHAIRWOMAN MOORE: There's no consideration of any kind of write-off, any kind of deal? That PG&E would get over the long run?

MR. GOLUB: Not at the numbers I was talking about is what I'm saying.

CHAIRWOMAN MOORE: I'm not dealing with those numbers. I'm dealing with the overall proposal to close down Rancho Seco which had to be based on an assumption that there be some write-offs and some other things that would be in it that would make it to your advantage to close it.

MR. GOLUB: To the extent there are write-offs, that would be a disadvantage that would be borne by the company's shareholders. That's not an advantage to us. That's a disadvantage to us to the extent there would be any.

CHAIRWOMAN MOORE: Let's go back to the write-offs not being an advantage. To the extent that you deal with the costs there and spread it out over your ratebase, that's not an advantage to you?

MR. GOLUB: I thought you were saying write-off would mean that it was not an item that would probably be included in the ratebase. That's what a write-off ordinary means, which means my shareholders would absorb it.

CHAIRWOMAN MOORE: Not necessarily.

MR. GOLUB: Maybe it's just terminology. To the extent there is a proper part of the price to pay, a reasonable part of the price to pay.

CHAIRWOMAN MOORE: I would assume you wouldn't make it if it wasn't the reasonable part of the price to pay.

MR. GOLUB: I'm assuming it too. If it was a reasonable price and the Public Utilities Commission said to include it, then it would be included in our ratebase and amortized over a long period of time.

CHAIRWOMAN MOORE: Is there any question in your mind that would not be a part, when you make the offer, wouldn't that be part of what you would be considering as you made that offer? That it would be part of the right price to pay, and if you had to close it off, it would be spread over the ratebase over an extended period of time? Would you recoup it from ratepayers?

MR. GOLUB: Historically, if the utility paid, what I call, too much of a premium for the acquisition of another utility system, the Public Utilities Commission does not allow that to be included in the ratebase. There are a long set of cases on it. It's not really controversial issue.

CHAIRWOMAN MOORE: We're not talking about you paying too much. We're assuming you are going to pay the right price.

MR. GOLUB: Then there will not be any write-off.

CHAIRWOMAN MOORE: If you closed it down, then there would be.

MR. GOLUB: Maybe terminology.

ASSEMBLYMAN LONGSHORE: Madam Chair, I have a question, if I may.

CHAIRWOMAN MOORE: All right, go ahead.

ASSEMBLYMAN LONGSHORE: We talk about incremental being that next kilowatt that you buy, making the assumption that next kilowatt will be available. Without Rancho Seco what would be the availability over time?

MR. GOLUB: You're quite correct. When you say that you must include an analysis of availability, and we did.

ASSEMBLYMAN LONGSHORE: Over time.

MR. GOLUB: Over time. We have significant resources in the PG&E generating system right now. We have access to purchased power at low cost. You can afford to buy low cost power on the spot market if you have a large reliable system to

back it up. You can't always depend on spot power being available. We have that nice mix which is a large stable base system, then we can deal in the marketplace in the Pacific Northwest, Southern California Edison and other utilities. This is a very conventional sort of thing.

ASSEMBLYMAN LONGSHORE: The problems on the east coast I wouldn't want to create on the west coast by not having in the future an incremental amount to satisfy the need.

MR. GOLUB: I agree. The analysis we did indicates that this is not needed for reliability for future users in the area. One of the toughest decisions, I think, businesses face is at what point you stop pursuing the investment you've made. It's a very hard decision. Psychologically it's a hard one and it is also hard to determine that point. But there is a point in some investments where that judgment has to be made. We're not saying what SMUD should do. We're saying if we were to consolidate with their system, it makes more economic sense to terminate the program and not put any more money into it.

CHAIRWOMAN MOORE: I'm going to let the write-off thing slide, because I still think I'm right. I think you would eventually put it in and it is offset by some other things. We are playing a semantics game here.

MR. GOLUB: It's not my intention. Maybe I can try to resolve it later.

CHAIRWOMAN MOORE: Some of the liabilities that are connected with closing the Ranch for SMUD are not there for you, including your own lawsuit against them and their inability to transmit, we are talking \$250 million that SMUD would be looking at that you don't have to face in closing. That has to be a consideration you would have that they don't have. What I really hope would be that we would be able to make a clear distinction why it is easier for you to come in and say close, as oppose to SMUD's inability...

MR. GOLUB: The basic answer is we have other resources available to us that are cheaper than the projected cost of the plant. They have analysis from their perspective of what resources they have available.

CHAIRWOMAN MOORE: I think those are the kinds of things we would be able to sort of set forth here, so it would become clear the decision is not as easy as people would like to see -- that SMUD could make the same kind of decision. Senator Greene?

SENATOR LEROY GREENE: You indicated the next kilowatt hour the cost to PG&E is 2½¢ per kilowatt hour?

MR. GOLUB: Projected over a levelized 20 year period. Yes sir.

SENATOR GREENE: You could plug the next customer into the line for 2½¢, which would create no profit to you, but that's what it would cost to deliver that kilowatt hour to that customer. Is that accurate?

MR. GOLUB: Yes sir, I think that's correct.

SENATOR GREENE: In other words, you would be delivering power at cost, at what it cost you to produce it, and there would be nothing for your shareholder in that 2½¢. Is that correct?

MR. GOLUB: That's right, because your fixed costs are already covered in the basic...

SENATOR GREENE: On the other hand what you seem to be guaranteeing the SMUD ratepayer is something like 7¢ per kilowatt hour.

MR. GOLUB: I have to check the number. You mean the rate freeze?

SENATOR GREENE: Your rate freeze, presuming that it includes the 8% that came up October 1, that put you at, plus or minus, 7¢, I believe. Is that correct? Just about 7¢?

MR. GOLUB: Yes.

SENATOR GREENE: So what you are saying then is that you can deliver to SMUD at your cost of 2½¢ and charge the SMUD customer 7¢. Now that logic is illogical or whatever. When that comes up tell me what's wrong with my thinking.

MR. GOLUB: I wish we were in that strong of a position, because I would then think the hearings would be relatively short if we had that strong a gap between the two. You have to realize that cost of producing power. That's the number comparable to the electron at the Rancho Seco powerplant. You have to get that from Rancho Seco or from wherever to the customer. You have

facilities to get it to the customer, transmission, but also, I think probably here pretty important, distribution. All the electric lines running down the street. You have to have people to maintain it, to repair it in the storm, and go out in the middle of the night. You have to have people to read the meters and prepare the bills. All those things. So, the cost of power that I was comparing at either 7¢ or 2½¢, both of those are comparable numbers. That's the electron when it leaves the powerplant, if you will or where you purchase it. Then you have to add in other costs. If we can deliver a product at prices radically below SMUD rates, this is something that would be very interesting in pursuing ourselves.

SENATOR GREENE: How do we see that until we see what the SMUD lost is. When we see that PG&E says' folks we will guarantee that rate and lower than that rate for an indeterminate, unspecified period of time? I don't know whether that is weeks, months, years or what it is, and I don't think you can tell me.

MR. GOLUB: Well, we said several years. The reason why we didn't put a number on the years, because we think that's part of the total package to be developed.

SENATOR GREENE: I can understand that. You are talking in years.

MR. GOLUB: Yes sir.

SENATOR GREENE: Let me ask you this question. What is an average rate, let's say, that you're charging some household customer in your system in some other town as it would compare to that rate of three or four years ago?

MR. GOLUB: Our rates have gone down a bit in the last two years.

SENATOR GREENE: In the last two years?

MR. GOLUB: Yes sir. We have shifted from...

SENATOR GREENE: Because of the lower price of oil or you shifted away from oil?

MR. GOLUB: Well, primarily, we shifted away, although the lower cost would help if we were still burning it.

SENATOR GREENE: You shifted away from oil and at Diablo, it cost you more than your oil fire plants?

MR. GOLUB: No. The operating costs at Diablo are a lot lower. The capital costs are higher.

SENATOR GREENE: That's your problem with Diablo?

MR. GOLUB: Well, with either a hydroelectric, geothermal or nuclear powerplant, your dollars are fixed. Your fuels are relatively inexpensive or free if it's water. With an old fossil fuel plant, your capital costs aren't as great, but your operating costs are high.

SENATOR GREENE: Thank you Madam Chairwoman.

MR. GOLUB: Do you want me to go ahead with the other points in the proposal?

CHAIRWOMAN MOORE: We were kind of check-listing the things that you thought were an advantage. Why don't you sum those up in three minutes for me?

MR. GOLUB: Point three was decommissioning. Point four was we would freeze electric rates in the area for several years.

CHAIRWOMAN MOORE: One comment on freezing rates, as Senator Greene was pointing out, you are freezing rates at an all time high for SMUD. I think that has to cause some considerable concern. As you also point out it is for an indeterminate period of time.

MR. GOLUB: SMUD is projecting a 37% increase in rates in the next year or two. So, I think that proposal would be attractive. Fundamentally, I think, all of this is a thing that has to be evaluated. If it doesn't make sense to the people of the area then they are not going to accept it. That's the fundamental point.

CHAIRWOMAN MOORE: That's why I'm raising a few questions as you move along.

MR. GOLUB: The fact is we would freeze electric rates in the area for several years. The SMUD employees would be assured job security. Governmental entities in the area would receive, we estimate, approximately \$15 million in additional tax and franchise payments every year. That's just money they don't get today that they would be getting. As I said our lawsuit, which has a very large contingent liability for SMUD, would be

resolved as part of this in the total transaction of the benefits to each party. The SMUD ratepayers would not have to face that in their rates, which would be, I think, what they have to face if PG&E prevails and gets a large judgment against SMUD. We would eliminate that additional upward pressure on their rates by settling the case as part of the transaction.

CHAIRWOMAN MOORE: Your ability to do that is also one of the reasons SMUD can't just close down Rancho Seco, because they wouldn't have the ability to provide the capacity required under your contract?

MR. GOLUB: I disagree. Let me explain our position. In litigation our position would be they failed to operate that plant in a proper way and resulted in a shutdown and they didn't bring it back up in a reasonable time period, which made us support their system. That's what our damages are for all that period.

CHAIRWOMAN MOORE: Of course, that's going to be a lawsuit that is going to be decided, but they are going to come back and tell you they have been spending \$20 million a month doing everything that the NRC has been telling them to do. They are going to come back and make those arguments. That's all what the court and the judge is going to have to decide.

MR. GOLUB: I quite agree, but the point is that is past liability and doesn't go with the question of shutting the plant down in the future. As to the future, our position would be that if SMUD wanted to close down the plant...

CHAIRWOMAN MOORE: We're going to play sematic games again. Would it not make your hands stronger in the court if it came to be that they had closed down their source of the power that they were supposed to be supply to you?

MR. GOLUB: It doesn't make my hand stronger. It makes my damages greater and I want to be compensated. There are alternative techniques if they wanted to explore that. They could choose not to be as dependent upon us, so I don't have to charge them. That's one solution. Another solution would be get replacement capacity for other sources. There are other sources. There are other solutions, but those have not been explored.

CHAIRWOMAN MOORE: There would also be the transmission for SMUD to make transmission available for some cheaper sources to come.

MR. GOLUB: The transmission of the economy enery would not provide a firm source of power. That doesn't solve this part of the problem. This part of the problem hinges on firm power as opposed to economy energy.

CHAIRWOMAN MOORE: You're telling me they couldn't go out and contract and maybe give the support to you at a lower rate?

MR. GOLUB: If they had a firm transmission patch that was available and they have a firm source of power, that is a way it can be done. Yes.

CHAIRWOMAN MOORE: Of course, the only transmission patch is yours.

MR. GOLUB: No, that's not true either, because there are several transmission systems including the Western Area Power Administration in Northern California. There is a proposal for a major project owned by a majority-owned of public entities, and moreover, the primary transmission facility that they are thinking about...

CHAIRWOMAN MOORE: Do those things exist today? But anyway, let's go ahead.

MR. GOLUB: Can I make one other point though? SMUD today has a contractual right to 200 megawatts on the intertie, the main transmission facility in Northern California. Two hundred megawatts, they have a firm contract right to that. They have more use of that intertie on a per capita basis than PG&E. We have the bigger share of it, but when you compare it against the source of our load as compared to theirs, they have a bigger share of the firm capacity on that facility than we do. Also about a year or two ago, they contracted away 50 megawatts of that to another entity. Now, I'm not going to be here analyzing their position, but it seems to me if they chose to contract away 25% of that, that is a decision they should live with, not look to us to make that up. We need that facility to serve our customers, our share of it.

Now, the key point I'd like to make in trying to wrap this up is, that the way to proceed here is to look into these questions, and they are difficult questions, in a business-like way, with the SMUD representatives meeting with ours to discuss the economics of all these things. These are all valid questions that are raised. I can't, in this time frame, go through each and prove each point. But, that's a point the negotiation process should address. That's why we want to proceed. On October 1, Mr. Clark made a very strong pitch for that. He asked that that be done. We would like to see a process begin immediately to evaluate the facilities, which is a key part of this whole debate, looking at the other economic questions in a real serious way, and not to run a delay. We observe there is a lot of money being spent in the restart effort. If the decision is later made that our proposal is the right one and should be accepted by the people of the area that's wasted money. It would be a shame to have that occur. So, we urge that kind of dialogue early on.

Finally, I would just like to say I think our proposal should be evaluated on the basis of its own merits and not distorted by this public power/investor-owned sloganeering. I don't think that really has anything to do with the real interest of anyone. I think they should look at the economics to see if it makes sense to the consumers involved for their system and our system, and analyze it on that basis. We think if it is analyzed

on that basis it would be found to be very attractive and very reasonable.

CHAIRWOMAN MOORE: Are you saying PG&E doesn't like competition?

MR. GOLUB: I'm not saying that at all. I'm saying that in a competitive environment, actually if you want to put that point on it, competitive, I assume means, you have a free choice by the consumer. In this case, the SMUD consumer. If he sees a better alternative, he should take it, and the economic system works better, because it keeps the efficiencies going forward in the competitive process. Some people seem to be suggesting that government-owned utilities should be immunized from this kind of competitive challenge. They should not be. This is exactly what you want to foster. Investor-owned utilities face that competitive challenge. There are annexations that occur all the time. SMUD on occasion annexes parts of the system of the area we serve. No one views that as somehow anticompetitive. It is used as part of the natural process. I would suggest to you the process only makes sense when it works fairly. That's to say that both entities have the opportunity to present to the voters, at least we have to present to the voters, annexation -- even though I'm not so sure we always have that -- the opportunity to decide. That's what's real competition is about, not building some kind of rule guaranteeing someone special treatment. That defeats competition. But, I don't really think you're talking

about competition here. You're talking realistically about the opportunity these people have to look at a proposal which we think makes a lot of sense.

CHAIRWOMAN MOORE: I'm going to let you have the last word.

MR. GOLUB: I think my last word will be thank you.

CHAIRWOMAN MOORE: Senator John Garamendi?

SENATOR JOHN GARAMENDI: Thank you very much for the hearing. It is certainly important to this area and thank you for taking the time to do it. The details of your proposal are not fully understood and I understand why they are not at this point. You don't have access to information and it is preliminary. Repeatedly in your testimony here, you have asked for a dialogue to take place. Is that now taking place?

MR. GOLUB: Not yet. We would like it to start it immediately.

MR. JOHN KEHOE: Let me state that the SMUD board in response...

CHAIRWOMAN MOORE: Please identify yourself for the record.

MR. KEHOE: I'm John Kehoe. I'll represent the SMUD board in a few minutes. But the SMUD board at the meeting on October 1 recognizing that in any negotiating process, factfinding must progress, has designated Frank Hahn as the leader of our team. He currently is in preparation of his team

to meet with the PG&E people very soon. But we do think it is imperative that the full details be disclosed as quickly as possible.

MR. GOLUB: At the SMUD board meeting, I think, there were a variety of views expressed. Mr. Kehoe can articulate the reasons. I only heard what was said. As I understood it, some board members wanted Mr. Hahn to get in touch with us for some preliminary decisions. Some wanted, I think, to delay to obtain outside attorneys. Other comments were about waiting for the general manager who has just been hired, give him a chance to start work and get familiar. I'm speaking second hand, so I don't have exact language, but there was a lot of that said. As we left the meeting, I think it was understood that Mr. Hahn would be in touch. When I left the office yesterday, it hadn't yet occurred. I gather it will occur soon.

SENATOR GARAMENDI: I'm going to come back to that point. It seems to me that it is in the interest of residents of the Sacramento area that this proposal from PG&E be thoroughly evaluated and all information be made available so it can be evaluated by both parties. Mr. Kehoe, when you make your presentation, I'd like to ask you some questions about this also, not only with regard to PG&E, but with other potential sources. Thank you.

CHAIRWOMAN MOORE: Mr. Kehoe.

MR. KEHOE: Good morning, Chairwoman Moore and members of this committee. My name is John Kehoe. I am a member of the board of directors of the Sacramento Municipal Utilities District. I too want to add my thanks to you and to this committee for taking the time and interest in this key subject.

I think the consolidation proposal which Mr. Clark made in his letter of September 3 presents a very radical change, not only for Sacramento, but for the entire utility industry statewide and even nationally. This committee's calling this hearing within days of Mr. Clark's letter suggests you too share this valuable perception. My remarks this morning are going to be very brief. I intend to provide you some background in describing the district and what the board of directors sees as its role in this matter. I then will introduce Mr. William Latham who is the acting general manager who will provide the district's current detailed perspective on the consolidation idea.

SMUD is a local public agency.

CHAIRWOMAN MOORE: You're not going to read that to me?

MR. KEHOE: What's this?

CHAIRWOMAN MOORE: Your statement?

MR. KEHOE: Well, I wanted to give you some background because I think it is important. The media looks upon SMUD locally as a continuing saga of the perils of Pauline. I wanted to go into some perspective from our point of view...

CHAIRWOMAN MOORE: You've been on that board long enough. I know you don't have to read that to me. Just give us a little background.

MR. KEHOE: I will submit this for the record, but there are a couple of key points that I think are essential to be made in this whole picture. One is we have been operating for 40 years. We were formed by a vote of the people in 1923, which is very critical for public power people to know. However, it took some 24 years to negotiate with PG&E on the subject of the cost and evaluation of the system. In other words, it took 23 years to put the money together, a valuation and the determination we were to be a public municipal utility district. For the past 40 years, we have been the distributor of electricity in this area.

In the course of 40 years, we have put together generation sources that we have relied upon; a very effective hydroelectric system, and a geothermal system. Rancho Seco was put on line after a number of years in planning and in construction. It is a 913 megawatt nuclear powerplant. Now, we have been in an outage situation over the last 21 months. They is expected to last another 3 or 4. This has contributed greatly to the rapid escalation of rates and to the weaking of the district's financial position.

Since 1944, our rates have increased from 53% to 89% of the PG&E base rate in the area surrounding us. Then we are faced with the notoriety that surrounding events of Rancho Seco have

increased the public's concern about the district to a high level, and no doubt contributed to PG&E's decision to propose consolidation at this time. Now, the problems the board has faced have been very seriously reviewed from the standpoint of how we deal with them. We feel that risk reduction -- this is a concept we've come up with -- is something that should be carefully considered. Risk reduction in our definition of this consists of four different approaches. Mr. Clark has added a fifth, namely consolidation. But nevertheless, the four we have looked at have had to do with the power supply solicitation efforts. This is the RFP that resulted in 50 proposals, totalling over 6 thousand megawatts of potential power, which taken singularly or in various combinations provide many different options for the district. We have looked at Rancho Seco. The position it occupies in the whole economic spectrum. We have also looked at the possibility of a holding company being formed which would take on the assets of the district and would manage them in combination were the other alternatives we were looking at. These four approaches, plus the fifth option of consolidation, are currently what the board is reviewing in the way of risk reduction.

Now, I would like to bring on Bill Latham for the technical response I think is vital for your concern. Mr. Latham has served very admirably. I want to take a minute to acknowledge his long and dedicated service. We called upon him

to be the acting general manager. He has served the district for more than a quarter of a century. I think it has been 26 years. He has been in 14 months as our acting general manager. As you know on October 1, we appointed Richard Byrne as our permanent general manager. Mr. Byrne comes from a long history of executive excellence in the field of public power. He's currently head of Massachusetts Wholesale Electric Energy Company. He will be arriving on November 1 to take over leadership of the district. But, I'm pleased to introduce Bill Latham.

MR. WILLIAM LATHAM: Thank you Mr. Kehoe. Good morning, Madam Chairwoman, members and ladies and gentlemen. I hear Mr. Kehoe's enthusiasm for the future of SMUD. Perhaps SMUD's view of the consolidation idea can be best understood in the context of our current situation.

Basically at the present, SMUD has major generation resources totalling nearly 1650 megawatts to meet its 1900 megawatt load. These are comprised of hydroelectric plants, nuclear plant, Rancho Seco, and we have 72 megawatts of geothermal steam electric, 49 megawatts of combustion turbine, and are currently building a dual 65 megawatt plant with other Northern California entities. In addition to that we have 360 megawatt long term contract with the Western Area Power Administration. Two hundred megawatts of firm transmission to the northwest as well as the integration contract with PG&E.

The PG&E agreement has been an integral part of the district's resource mix. In general terms the contract really calls for the sharing of the economy of a large scale plant associated with Rancho Seco. PG&E would benefit from purchasing SMUD's surplus firm capacity and energy at SMUD's production costs which are less than PG&E alternatives.

The principal feature of the contract is that the parties share reserves. So in the event of an outage of either generation or transmission, the resources of the entire innerconnected system are available to meet the loads of both systems. PG&E purchases nearly all the capacity and energy that are surplus to the district's needs or requirements. This allows the district to operate its resources -- all of its resources, not just its nuclear resources -- at very high capacity factors so that the cost per kilowatt hour can be held to a minimum. The district's generation is less than its requirements. PG&E makes capacity and energy available on an exchange basis to the district. The energy that is provided is subject to annual energy borrowing limits, and if we go beyond those limits, there is a cash payment requirement. This agreement has been amended twice, and it expires in December 31, 1989.

The contract states that the parties will attempt to negotiate a long term interconnection contract. If that fails, PG&E is required to file with Federal Energy Regulatory Commission a new rate schedule under which PG&E will provide the

district the services that the district needs after December 31, 1989. As we mentioned earlier, there is the litigation of the current contract in front of the Federal Energy Regulatory Commission.

The outage of Rancho Seco Nuclear Powerplant has caused PG&E to focus primarily on that plant, and to seek a unilateral change of the terms of the integration contract. This, of course, has resulted in litigation. In February 1986, PG&E notified the district that it would no longer make payments to SMUD as required under the contract for Rancho Seco capacity until Rancho Seco was restarted and operated reliably.

CHAIRWOMAN MOORE: When did that letter come?

MR. LATHAM: That was in February 1986. PG&E has also told the district that PG&E believes the rated capability of Rancho Seco has changed from 913 megawatts to 0. The district believes the current Rancho Seco outage constitutes a short-term curtailment within the meaning of the contract. The contract is very clear on this issue. Short-term curtailments are not a basis for re-rating of Rancho Seco under the contract if the district uses due diligence to return the plant to service. The district is meeting this obligation.

In 1986 the district filed a complaint with the Federal Energy Regulatory Commission asking for a ruling to that effect. The dispute is exceedingly complexed. Although PG&E may disagree with the number, we believe that realistically approximately \$22

million in capacity payments are at stake. Additionally, if SMUD loses, SMUD must deliver to PG&E substantial quantities of surplus capacity, which SMUD will have available in its offpeak months. The FERC proceeding is now on trial in Washington, D.C.

We have heard about the district's financial rating and how that has changed, and it certainly has. Over many years of extremely strong financial conditions, the district held a AA bond rating. The district has most recently reported loses of \$9.2 million in 1985, \$3.7 million in 1986, and had a corresponding gradual lowering of the district's bond rating to now a BBB rating. The extended outage of Rancho Seco has a major impact on the district's financial and operating condition, resulting in increased operating and maintenance expenses to restart the plant and additional purchase power requirements. At the same time, we had a decrease in income from the sale of surplus energy from Rancho Seco. With the restore of Rancho Seco at hand and the results of recent actions of the district to restart financial health, our financial picture has stablized. Net income for the first half of 1987 is \$8.7 million. We have an annual projection for 1987 of \$12 million. The district's liquidity through 1988 is assured with the sale of \$150 million bond issue executed just last week. So, we feel that the financial picture is brighting.

The 1987 budget is \$832 million, which includes \$240 million for the restart of Rancho Seco as well as \$200 million

for purchased power costs. The original 1988 budget requests is for \$750 million.

CHAIRWOMAN MOORE: Mr. Latham, I have been letting you do something that I normally do not let people do and that is to read to me. Why don't you try to sum it up, so we can kind of move on. I have a long hearing.

MR. LATHAM: You certainly have. Basically our 1988 budget is 9 to 10 percent below the 1987 budget. This provides you with an overview of the current financial situation of the district.

Let me talk about the future. We have look at what has been talked about here as a risk reduction program. The board last year directed the staff to look into alternatives regarding the lowering of its operational and financial risk associated with a large plant. As a result of that direction, we have come back with four alternatives. We can operate Rancho Seco selling a portion of its output. We can transfer the ownership and operation of Rancho Seco to another utility. We can reconfigure the electric system or we can repower Rancho Seco. Under the senario of operating Rancho Seco and selling a portion of its output, that would, under the current agreement with PG&E, end in 1990. At that point in time, we could enter into contracts with other utilities for either exchanges or sales of surplus power. The transfer of ownership and operation of Rancho Seco falls into another area of interest. The district recognizes that the

potential transferee would assume ownership of Rancho Seco, but that would be over a short period of time. It would not be immediate. The transferee would want to operate the plant from 2 to 4 years before they would want to accept the plant in total. We still believe that is an option that we're pursuing with great diligence.

CHAIRWOMAN MOORE: Have there been offers to take over the operation of Rancho Seco from anyone?

MR. LATHAM: Yes, there has. There has been one noted in the newspapers quite frequently, the Duke Power Company of North Carolina which operates seven nuclear plants. Three of them are sister plants to Rancho Seco. They have an extremely good operating record, and they are interested in assuming ownership of Rancho Seco, but not immediately. They are suggesting a 2 to 5 year operating agreement at the end of which they decide whether they wanted to assume ownership.

CHAIRWOMAN MOORE: So basically you would transfer the operation to them and you would still own it?

MR. LATHAM: That's correct, and be responsible for the operational and financial risks. We would still maintain the license.

CHAIRWOMAN MOORE: Senator Garamendi?

SENATOR GARAMENDI: Who would oversee the utility's operation of that plant if SMUD doesn't own it? The PUC? They are a wholesaler of power and I don't know if they come under the PUC authority.

MR. LATHAM: They would not. As we view the laws if someone like Duke would assume ownership of the plant, then they would be controlled by the Federal Energy Regulatory Commission.

SENATOR GARAMENDI: Then there would be no control at all from within the State of California?

MR. LATHAM: That's correct.

SENATOR GARAMENDI: Isn't that interesting?

MR. LATHAM: The license would be controlled by the Federal Nuclear Regulatory Commission of course.

SENATOR GARAMENDI: We worked with them before?

MR. LATHAM: Yes.

SENATOR GARAMENDI: Thank you.

CHAIRWOMAN MOORE: Assemblyman Connelly?

ASSEMBLYMAN CONNELLY: I have a question that relates back to the discussion I had earlier with PG&E. It's my understanding the board recently authorized the solicitation of bids for electricity not to exceed 4.2¢ per kilowatt. I believe that's the figure.

MR. LATHAM: That's correct.

ASSEMBLYMAN CONNELLY: You have received offers equal to 6 thousand kilowatts, of which some may be valid, and some of which are a variety of different things. I assume and maybe I'm incorrect, there is a basis for that 4.2 figure and that is it has some relationship with the cost of getting the similar amount of electricity from Rancho Seco over a similar time? I just asked that as an initial question.

MR. LATHAM: I'm not prepared to defend that.

CHAIRWOMAN MOORE: Before you do that, one of the options he is going to evaluate as he moves through is that whole source of power.

ASSEMBLYMAN CONNELLY: I'll just plant that question with you, and when you get to that, you could answer it.

MR. LATHAM: If I could answer that question, that number was proposed by a board member. That board member is willing to defend that number. It is not one that the staff necessarily has support for.

ASSEMBLYMAN CONNELLY: Staffs?

MR. LATHAM: We can develop a number of issues to support that.

ASSEMBLYMAN CONNELLY: So the board member figure of 4.2 and PG&E is saying 7¢. What is staff saying?

MR. LATHAM: There are a variety of alternatives depending on what they were talking about, incremental costs or imbedded costs.

ASSEMBLYMAN CONNELLY: I'm talking about the cost per kilowatt from Rancho Seco.

MR. LATHAM: The cost per kilowatt from Rancho Seco is about 4.2¢ per kilowatt hour. That depends on its capacity. That's assuming the capacity factor of approximately the national average for that kind of plant.

MR. KEHOE: Isn't it the concern of the staff that it should be less than the figure that the board has chosen, is that the difference. I didn't want the committee to be left with the feeling that it would be higher.

ASSEMBLYMAN CONNELLY: My concern is that the PG&E figure seems to be such a different point, and the board is making some decisions based upon a much lower figure -- 4.2, I guess, conceivably lower -- that to reconcile a 75% difference in the cost, seems to me to be important. Let me tell you what the fear I have. The fear I have is there are 6 or 7 options out there. Some of which look better than others. None of which, based upon information I have seen, are at the point where reasonable people can make reasonable decisions which one of them are the best. About one-half of them are or at least a good number of them, are credible options that include not continuing the operation of Rancho Seco. I'm concerned that we're making the decision to foreclose all those options which may in fact be the right decision on the assumption we can get 4¢ or whatever it is out of Rancho Seco and in fact we can't. What bothers me, not meaning to demean your projections on your ability to crank up Rancho Seco, but there are at least another six months of \$20 million a month and maybe more -- maybe considerably more -- and we could be a position where not just for the last year and half, but for the next year, we continue to spend \$20 million a month restart Rancho Seco when actually the best option in terms of

electricity for our community is an option that doesn't involve the operation of Rancho Seco. This is totally aside from those who are pro or con on nuclear power. All I'm talking is money. You know? I'm just talking money.

MR. LATHAM: We couldn't agree with you more.

ASSEMBLYMAN CONNELLY: I guess, then, what I need is some assurance that there is a specific hard plan, and the Senator made this point in our conversation, a specific hard plan to evaluate all these options fast, because it's a million dollars a day for us to scratch our heads. Then to make some preliminary decisions, when you look at the PG&E engineering report and 12 other things that I don't even know the right questions to ask, and then say, based on the fact we have 6 thousand kilowatts at 4.2¢, we shouldn't include Rancho Seco as an option economically at this point or we should, but we make that decision soon. I'm not saying that's not occurring, but at least based on press, I'm not persuaded that that's occurring.

MR. LATHAM: Chairwoman Moore perhaps I should elaborate at this point, that next Thursday evening at 7:30, the board is going to have a public meeting to evaluate outside consultants who can help accelerate this. The old saying, "you can't see the forest for the trees" we feel outside consultants would be helpful to accelerate the process to do exactly what Mr. Connelly is suggesting. In addition, we have appointed an advisory cabinet of senior Sacramentans, not necessarily in age but from

experience, that consist of a former colleague, Senator Rodda; Gordon Schaber, the dean of a law school, John Moss, the former Congressman, Frank Richardson, a former Supreme Court Justice; Justice Carr, who currently sits on the Court of Appeals for the State who is a distinguished lady in our community. These are people are going to help us evaluate the findings of these consultants.

ASSEMBLYMAN CONNELLY: Unfortunately the issue is so politically charged that sometimes it is difficult to take actions that may be reasonable actions, because they take on a broader significance. But, is one of the options being considered a slow down? Excuse me for suggesting this. It's so radical. But a slow down in terms of cost expenditure at Rancho Seco for the next 120 days moving from \$20 million a month to \$5 million a month until we get to the point that we make the decision that in fact is the proper economic decision to be made. I don't know. We're talking 6 months, \$120 million. \$120 million in the Legislature will stop the state budget for five days. People will yell at each other. We scream. We locked each other in the room. It's big money. My thought is, is there some way until we make selection of options that we can slow down the expenditure of that fund that makes good economic sense; or is that stupid, because the point of fact is you lose more than you've gained by cranking it back up again if you say you don't want to go?

MR. LATHAM: That question is an excellent question. It is one we are addressing and will be presenting to our board. We had intended to present to our board at the last board meeting, but unfortunately, with the presence of Mr. Clark...

ASSEMBLYMAN CONNELLY: So, what you're going to do at the next board meeting, there will be a specific staff evaluation on the issue on whether or not it makes sense to keep going at this point toward a restart, or whether we should slow that down pending the evaluation of these options which have surfaced?

MR. LATHAM: There is a study that will be presented to the board very quickly. We call it a wind-down scenario, and there are 3 or 4 alternatives there basically to take the plant to a safe condition and maintain its marketability.

CHAIRWOMAN MOORE: As you do that, since we don't seem to be moving through the evaluation of various options that are available to you, does your commitment to restart preclude the El Paso proposal for a gas fire or to refigure the powerplant?

MR. LATHAM: No, it does not. That is certainly one of our options that we're looking at very seriously. It has some real benefits. It has some real significant uncertainty because of the environmental problems relating to air quality.

CHAIRWOMAN MOORE: In pushing towards the restart, the expenditures, as we talk about this \$20 million a month, you have already spent close for \$400 million?

MR. LATHAM: Yes, it must be close to that.

CHAIRWOMAN MOORE: Or it may be a little lower if you only have three or four months left in it. So at this point, it still seems to be a viable option to back off all that money -- a half billion dollars -- you have spent to get Rancho Seco in a position to restart?

MR. LATHAM: Yes. We will show you what the impact is; really, the bottom line is the rates to the ratepayer. That is really fundamental.

CHAIRWOMAN MOORE: I think that would be real important. Why don't you just go real quickly through some of the options?

MR. LATHAM: Certainly.

CHAIRWOMAN MOORE: So you're saying that repowering is still a viable option?

MR. LATHAM: Well, it is one that has to be considered amongst all of the options. In addition to that the other option is the restructuring of the entire district's resources. That is turning the resources of the district, hydroelectric, steam generation and Rancho Seco, over to a holding company. Let them operate it and sell back to the district capacity and energy as the district needs it under some agreed upon price. So that's also an alternative.

CHAIRWOMAN MOORE: In your dialogue with PG&E will you be attempting to negotiate some access to transmission to all these cheap power sources and all these other things that you're getting? Are you going to be trying to negotiate with them?

MR. LATHAM: We sort of intend, as you may know, Mr. Jura of the Bonneville Power Administration, the administrator, already sent a letter to Mr. Dick Clark of the PG&E company asking Mr. Clark to work with him to figure out ways to deliver the northwest energy and capacity to the district. We recently sent a letter to PG&E asking them to consider transmission access for the responses to the request for proposal we had out that drew the 6 thousand megawatts.

CHAIRWOMAN MOORE: Does PG&E have that in its list of things to discuss with SMUD?

MR. GOLUB: We already stated on several occasions. I believe it carried against on October 1 that of course we would consider it. What you have to recognize is that the intertie which is the facility that we're talking about is typically pretty fully loaded. It is used by each of the entities that has a share. Now, SMUD has a 200 megawatt share already. Now they are talking about utilizing the shares of the other utilities such as PG&E, and as Mr. Clark said, we will explore that, but I will indicate to you that it tends to be pretty well utilized by our customers most of the time. But we will look into it and work something out.

CHAIRWOMAN MOORE: Have you thought about updating the sytem, which I think everybody has agreed, that if it were updated and brought up to par it should have increased capacity and would be able to accommodate?

MR. GOLUB: There is a project to build a third line to the northwest. The municipal utilities in the area have a majority ownership in it. The investor-owned utilities in the state who serve far greater role to have a minority interest in that third line. That's a project that's being worked on right now. I believe SMUD is a partner in that project. PG&E is and a number of other entities.

Mr. Longshore?

ASSEMBLYMAN LONGSHORE: If SMUD feels selling the facility a viable alternative or at least one to be considered, why is it that PG&E did not make the same consideration? Why is it they were so quick to, let's say, just tear it down?

MR. GOLUB: Their request for proposal on that subject was what triggered our analysis here. We did look at that question. We concluded that we are not interested in purchasing that plant.

ASSEMBLYMAN LONGSHORE: Somebody else is interested in purchasing that plant?

MR. GOLUB: Yes. I may have misunderstood your question. I thought you were asking me why we did not make an offer. The answer is we didn't.

ASSEMBLYMAN LONGSHORE: Your statement was we will take over and tear it down and close it up. That becomes a cost to you. The other viable alternatives is to sell it intact to another corporation. Why did you not consider that same alternative?

MR. GOLUB: We considered it and rejected it. The reason we rejected it is as follows: We believe as I said earlier, we have cheaper sources of power available to us right now. Why buy a more expensive item?

ASSEMBLYMAN LONGSHORE: You are still not answering my question. The question is, I have a plant here. I can either incur the cost of tearing it down, or I can sell it to somebody. Then it becomes an asset rather than a deficit. You don't want the competition?

MR. GOLUB: Yes sir. I'm trying not to criticize their project. I guess what I'll say if you force me to, I don't think the project has an economic value of the sort that you just describe.

ASSEMBLYMAN LONGSHORE: I have a house. It may be in shambles...

MR. GOLUB: Well sir, if your house contained spent radio-active materials and you had to spend \$1.5 to \$2 billion...

ASSEMBLYMAN LONGSHORE: But maybe I could get hard cash for it.

MR. GOLUB: But who would pay you hard cash for it if it had that large liability as part of the deal. That's a big part of the analysis. It's like if you sold a house which had some defect, the guy had to fix, the fixing up cost is more than the value of the house, he is not going to rebuild the house. He would tear it down and build a new one. That's an analysis each entity has to go through.

ASSEMBLYMAN LONGSHORE: You're precluding the man from making an offer?

MR. GOLUB: We're not precluding anybody from making their offer. Our analysis was that offer doesn't make sense from our perspective. Duke, as I understand it, made an offer. The other thing, I think, you're missing something. There is not, as I understand it, they really haven't offered to purchase it. They have offered to operate it for several years. The economic risks during that period will be left on SMUD. At the end of the period, I don't know the details of the proposals, they will decide whether they want to buy it. That's really very different from a contract to agree to buy a house. You pay to rent your house out for a while and I'll manage it for you. In a couple of years, I will let you know if I want to buy it. I don't know if they will decide in a couple of years from now. I know what we have decided. The final point I'd to make, I'd like to read to you something from SMUD's perspectus which they put out on September 18. I think this really captures a lot of it.

They are talking about the restart program, and they stated in this public document; a very important one. I'm sure they looked at the wording very carefully. "Therefore, no assurance can be given as to whether or when Rancho Seco will return to operation. Or if it returns to operation that it will not be required to taken out of service as a result of the initiative." And they go on to say and I'm quoting, "And no

assurance can be given as to whether further upward revision in the revised restart project will be necessary."

ASSEMBLYMAN LONGSHORE: So you are in effect correlating, placing, the closing of it strictly on political terms rather than the customer?

MR. GOLUB: No sir. Absolutely, the opposite. In economic terms what they are saying in this paragraph is they will try to work to get it restarted. That's their lead-in. They are going to make an effort to do so. Then they go on to warn the readers to say -- they discuss the requirements of the Nuclear Regulatory Commission, the Institute of Nuclear Power Operations and the insurance companies behind these various projects. So, they have their requirements. They say, therefore, no assurance can be given as to whether or when the plant will return to operation. That's problem one. They don't really know if they can get it back. Point number two they say, if they do get it back, we can give no assurance that it won't be shut down because of the initiative -- the political thing. There are two separate items. Then finally they say, point three, no assurance can be given as to whether further upward revisions in a revised restart will be necessary. These are three very important warnings they are giving the reader. Then they say this is a very formal document. I'm sure they thought it through very careful. They are being very candid in identifying some very, very major risks. Now, when we did our

analysis, we had those kinds of points in mind. I'm trying to answer your question without criticizing their project.

CHAIRWOMAN MOORE: I think the question that he's asking is clear. It just he wants to know if you have explored all the options available before your reached your decision?

MR. GOLUB: Yes, we did.

MR. LATHAM: Chairwoman Moore, he's reading from our latest bond perspectus. I'm sure you do know that the restart of Rancho Seco is contingent on several regulatory agencies as well as the insurance company.

CHAIRWOMAN MOORE: Mr. Garamendi, and then we're going to move on, because we have long panels before us.

MR. LATHAM: The consequence of that is it is very difficult to commit them, the regulatory agencies, to assure that there would be a successful restart.

MR. KEHOE: We have to very candid to the bond buyers as to what the exposure might be in this entire process. That's why they disclose so much in that document.

CHAIRWOMAN MOORE: I think that's generally understood. Mr. Garamendi?

SENATOR GARAMENDI: I have two basic questions. The first deals with your proposal to create a holding company. You did mention what you perceive to the advantage of that proposal and why it is being pursued.

MR. LATHAM: The advantage of that proposal is we could take the features that are causing the operational and financial risks of district, principally in a nuclear powerplant, and transfer those over to a holding company who would then assume those risks. It happens in that configuration the holding company would prefer to have all of the resources. They would pay back to the district certain monies. Then there would be a contract for supplying capacity and energy to the district out of those resources on a long term basis.

SENATOR GARAMENDI: That might lead to the operating system where the operations of those resources would be outside of the control of anyone in California?

MR. LATHAM: That's correct. Those would be under the control of the FERC.

SENATOR GARAMENDI: Thank you for that. Now the next question has to do with the one I raised earlier to PG&E. That has to do with the openness of the flow of information between SMUD and PG&E for the evaluation of their proposal. Could you comment on PG&E's statement a moment ago that as of this moment no meetings have taken place and there has been no discussion of the details that would underlie the proposals?

MR. LATHAM: There has not been, to my knowledge, any specific meetings on the basis of Mr. Clark's proposal last week. I would point out there has been quite a large number of meetings between the district and PG&E on the new interconnection

agreement which is moving forward. And the response to the RFP, which PG&E did respond to, part and partial of the list of options we're looking at, in addition to that discussion on transmission.

SENATOR GARAMENDI: What is the policy of SMUD with regard to investigating and providing information in regards to PG&E's proposal?

MR. LATHAM: Basically, the district is obligated to provide any and all information that it has in its files to anybody, and we have done that. We have a number of filings in front of the California Energy Commission.

SENATOR GARAMENDI: Let me back away and come at that a different way. I think that's not my question. When will you be meeting with PG&E? Is it your policy to meet with PG&E to discuss the details of their proposal?

MR. LATHAM: Absolutely. They are one of several options.

SENATOR GARAMENDI: When will you be doing that?

MR. LATHAM: We're hoping the board will approve of some economic evaluation support this Thursday. Once that's concluded, then we will be moving probably in the next week to meet with them.

SENATOR GARAMENDI: Is it the management's policy to pursue the PG&E negotiations as ardently as you are pursuing the other five options you have presented to us?

MR. LATHAM: It would be management's intent to do that, yes.

MR. KEHOE: And it would be the board's support of management to do that as well.

SENATOR GARAMENDI: I'm sure we will all be interested in seeing that occur. Thank you very much.

CHAIRWOMAN MOORE: Let me thank you for your comments. We are going to move on to the next panel. Mr. Polanco has a question.

ASSEMBLYMAN RICHARD POLANCO: You mentioned a holding company and in the prospectus -- I quickly glanced through it -- there was not made mention of the holding company, is there a reason why?

MR. LATHAM: It should have been in there. I'm not sure how it was described, but it should have been in there.

MR. KEHOE: I think it is under the risk reduction section in there.

CHAIRWOMAN MOORE: Probably one of the five options that I think they talk about in there.

MR. KEHOE: Chairwoman Moore, I would like to introduce two elected board members who have been in the audience. I assume they are still there. Anne Taylor and Ed Smeloff. Anne is one of the more senior members and Ed is one of the more junior members.

CHAIRWOMAN MOORE: I have been reading their comments lately.

MR. LATHAM: I have two charts which I would like to show you.

ASSEMBLYMAN CONNELLY: I wish we could put both of them on the same panel, that would have been great.

CHAIRWOMAN MOORE: Why don't we move on, because we do have a long agenda. I hope you will stay around, because there may be questions that may come directly back to you. We are going to move into the second panel. I'm not going to ask PG&E and SMUD, because one of the things that we had planned to do at this time is to review the options that were available to you. I think we have kind of done that at length and some of economics of that deal. So, why don't we move to Jerry Jordan from the California Municipal Utilities? I'm sorry, I need Greg Cook first and Mike Remy. Let's do those two. Mike Remy, Sacramentans for Safe Energy.

MR. GARY HIRSCH: Madam Chairwoman, my name is Gary Hirsch. I'm not Mike Remy. He is in Europe. It is a long trip for him to come back, so I am appearing for him. I'm a member of the Sacramentans for Safe Energy (SAFE) board of directors. I was a member of the Sacramento Municipal Utilities District's board of directors for 1976 to 1980.

It is the history of SAFE that some time ago they foresaw some of the problems we are presently having to deal

with. It was their proposal to try and put an initiative on the ballot which would make the decisionmaking process in the hands of the ratepayers and the voters of Sacramento as to whether or not to continue to operate Rancho Seco as a nuclear facility. I'm sure you are all aware there was an initiative circulated and 50,000 signatures were obtained. It qualified in May. There was a decision recently as a result of the lawsuit to put that initiative on the ballot in June of 1988. I think it is important to take into consideration that the initiative has some very specific provisions. That is Rancho Seco can not continue to be operated as a nuclear facility until there is approval of the ratepayers to do so. In addition, the SMUD board can not sell, lease or get rid of the nuclear facility without approval of the ratepayers and voters. I think those are two important provisions to keep in mind when we look at what is happening today, and some of the decisions that are potentially being made as to what to do with Rancho Seco.

CHAIRWOMAN MOORE: The provisions that you just described, is that the specific language as it will appear on the ballot?

MR. HIRSCH: No, let me read that to you. Section 2 of the initiative specifically states...

CHAIRWOMAN MOORE: Section 1 does what?

MR. HIRSCH: Section 1 says the ordinance shall be cited as the Rancho Seco voters rights initiative.

CHAIRWOMAN MOORE: Okay.

MR. HIRSCH: I'll read to you what I think are the pertinent sections. It is the policy of Sacramento Municipal Utilities District not to operate or permit the operation by others of the Rancho Seco Nuclear Generating Station for the purpose of generating electricity by the use of nuclear power without the expressed approval of the majority of the voters of the Sacramento Municipal Utilities District. Voter approval is required to continue to operate as a nuclear facility.

In Section 5 it says the Rancho Seco Nuclear Generating Station shall not be sold, leased, or otherwise transferred to any person, corporation, public agency or other legal entity for the purpose of generating electricity by the use of nuclear power until such sale, lease or transfer is authorized by the express approval of the majority of the voters of the Sacramento Municipal Utilities District.

CHAIRWOMAN MOORE: So the options we have been exploring this morning with possibly of having it gas fired would still be an option available to them, in terms of what they can do, as opposed to transfer or lease?

MR. HIRSCH: Absolutely. That's correct.

CHAIRWOMAN MOORE: One other question along those lines. There is nothing in the initiative that speaks to, if the initiative is successful and Rancho Seco can no longer be operated, there is nothing in there that gives any direction on how they are to phase it out or close it out?

MR. HIRSCH: No, it doesn't address that. I think what is pertinent is what happens between now and the vote of the people. What if certain actions are taken by the board of directors of SMUD with regard to transferring to a holding company and with regard to the PG&E offer? Those are very important considerations. Are we subverting the request of the people to vote on this matter? And, I think those are important issues that have to be discussed and decided, whether there is going to be any action taken prior to the vote on this initiative.

CHAIRWOMAN MOORE: So your belief, and I guess the belief of the SAFE group, would be that the board is not in any position to take any of the options that leads to the continuation of the operation of Rancho Seco at this time?

MR. HIRSCH: Yes, that is the position of SAFE. We want the voters to make the decisions, but I'm not sure the ...

CHAIRWOMAN MOORE: You can only speak for yourself. I'm not asking you to anticipate what the SMUD board is going to do. Basically, your position is clear. At this time if you had your druthers they wouldn't do anything else until the vote is taken in terms of making any decisions regarding the Duke offer or any of those others?

MR. HIRSCH: That's correct. I think if you look at hindsight and almost two year ago before \$400 million was spent, if you ask people would they had spent \$400 million to be in the

position we are in now financially for SMUD or to have that \$400 million and shut down Rancho Seco back then, it would be a very interesting question, and the people would have to decide.

CHAIRWOMAN MOORE: Well, I think if you put that through the hindsight twenty-twenty, I think the board would probably share your view, in all fairness, I think they would probably agree maybe.

MR. HIRSCH: But it has been over a year that the SAFE board has been requesting that. We have been ignored. We have been ridiculed and told we don't know what we're talking about. That's what's of concern to me. Maybe there is another viewpoint that should be considered.

CHAIRWOMAN MOORE: Mr. Connelly.

ASSEMBLYMAN CONNELLY: Your question, Ms. Moore, brought out the point and that is because the initiative is not retroactive the board could defeat the intent of the initiative by taking action to sell Rancho Seco. I wanted to make sure everyone understood that.

There are conflicting public policies if they continue with the restart effort which costs \$20 million a month. If it is not a good decision to restart it, then it's advantageous for them to make a decision as early as possible, which in part is why I tried to explore that. It is difficult to know whether or not there is some interim process that can occur pending the analysis of these options and ultimately the vote of the people.

CHAIRWOMAN MOORE: Let me ask you something. Have you explored with legal experts, so to speak, the implications of the initiative if SMUD does take such action prior to the vote of the people?

MR. HIRSCH: No, that has been researched. I am by occupation an attorney. I think it is a very interesting question. I don't think it has been addressed nor there is any legal authority, but I think there would be an argument that had to be made. I think the argument is that the board of directors of SMUD has fiduciary obligation to the ratepayers. Whatever action they take they are responsible to abide by that obligation that they have undertaken when they assumed office. I don't think there is any case law directly on point on the issue, but it is certainly very interesting legal question.

CHAIRWOMAN MOORE: One of the things we might be interested in taking a look at is to see if there is any legislative precedence anywhere in terms of this kind of activity taking place where there is a pending voter initiative.

MR. HIRSCH: If I can continue very briefly? I don't have much more in comments.

CHAIRWOMAN MOORE: Sure.

MR. HIRSCH: The PG&E offer from the perspective of the SAFE board, we have no position. I guess it is sort of dichotomy there. We accept the fact that PG&E is saying to shut down Rancho Seco. We should be all in favor of the PG&E offer. On

the other hand, if you believe in public power and the economies of public power, we are against such an offer. If you look at it over the long spectrum of time period of 20 to 50 years, is it in the best interest of the ratepayers? But I do think the one thing that is important in the offer is the validation of the opinion we have had for some time and that it is no longer economically feasible to continue to operate Rancho Seco. And, to briefly respond to Mr. Longshore, the other element that I don't think was addressed by the other gentleman from PG&E -- it is my understanding members of SMUD can correct me if I wrong -- why Duke Power is interested in taking over this lease arrangement is that there is a guarantee that SMUD will purchase a percentage of the power from Rancho Seco. So, they have a guaranteed customer. Whereas PG&E does not have guaranteed customer if they were to operate the facility. So, that is where the difference, I think, comes into play between PG&E and Duke. Duke has a win-win situation. They don't have to pay for the operating cost during the lease period is my understanding, and they have a ready customer in the SMUD ratepayers, but that cost may be higher to the SMUD ratepayers than would be on the spot market or on the other markets.

ASSEMBLYMAN LONGSHORE: My concern is more on the availability of power. With the possibility that the federal government has built all the dams they will ever build, with other kinds of electric power sources being curtailed by

environmental considerations and other things, I'm wondering what's going to happen at the Year 2025 or the Year 2030 or 2040 as to the availability of electric power? If we preclude the use of nuclear power, if it is a safe function, then it should be pursued. Your assumption that it is a lose-lose situation is premature in the respect that those that are operating can not say that at this point in time. They are studying it. They haven't come up with it. They have it as a viable option to consider: study. They haven't made the decision whether to reopen. They are trying to repower. They are spending \$20 million a month, as I understand doing that. But I think the cost of maintaining an asset in a condition which makes it a saleable product. The fact that the initiative carries not only "you can't operate it" but also "nobody else can operate it, and you can't sell it for anybody else to operate it" precludes the use of the power function from now until eternity. I think that is not a choice that should be made by a local entity in its entirety, because you are making a statement which has national scope as well as local scope. I think the consideration should be made only after all the facts are in. At this point all the facts aren't in. So, your assumption that it is a lose-lose situation, I think is premature.

CHAIRWOMAN MOORE: Well, I think that one of the ways that makes this country great is the fact that he does have the initiative and he can take it to the people, and they can make

that decision. Why don't we have you finish, then we will go to the NRC, and take further questions from the members.

MR. HIRSCH: Fine. Finally with regard to the PG&E offer I think what's under the surface and hasn't really been stated is the historical animosity that exists between PG&E and SMUD, and that would cause me to wonder whether or not SMUD would give an objective evaluation of the PG&E offer. You had 30 years of wars between PG&E and SMUD when SMUD was trying to be established in the first place. I believe that's evident by the legal disputes that are currently going on between the two entities. I think that factor must be taken into consideration.

With regard to the holding company and the Duke offer, it is my understanding and again, I will be corrected if I'm wrong, that as a part of that there is another utility in the State of California, Southern Cal Edison is a part of that holding company or has an interest. I think that is important to you, then that brings in the element of competition with PG&E and has certain an effect on PG&E were Southern Cal Edison to come into the Sacramento area.

CHAIRWOMAN MOORE: That has lots of interest to me.

MR. HIRSCH: I think the final thing I would like to say is this is a very complex and a very controversial issue. I don't know if we are all going to agree, but when we leave this room, both... What I do think is important is to form this district it took the approval of the ratepayers. And to sell the

assets and to dissolve this district, I think it should again take approval of the ratepayers. Thank you.

CHAIRWOMAN MOORE: Thank you for your comments. Let me ask you just a couple of questions. Let's talk a little economic realities. The economic concerns are not what SAFE is about? Is that correct?

MR. HIRSCH: I think it is a motivating factor. You have many issues that are of concern: safety, the nuclear waste, the nuclear power, and the economics. I don't know how you can separate those.

CHAIRWOMAN MOORE: I guess the position of the initiative is one that's very clear: that there is not to be any further operation of the nuclear power at Rancho Seco. There is going to be some cost in closing it down and the decommissioning that is going to have to be borne by the ratepayer. The question I'm really asking is: is it a consideration that there may be considerable cost tied to the initiative?

MR. HIRSCH: Yes, but that cost would have to be incurred eventually anyway. The thing that is very interesting about that point is in the SMUD budget, I believe, for 1986, they put the cost of decommissioning at \$118 million. I've heard Mr. Clark from PG&E say \$230 to \$280 million. I thought somebody here today say \$1.5 billion to \$2 billion.

CHAIRWOMAN MOORE: They did say that.

MR. HIRSCH: There is a little bit of disparity between those numbers. Yes, that was a consideration.

CHAIRWOMAN MOORE: One of the things that we talk is in today's dollars and at the time the decommission is complete, and the billion represents at some 20 years, maybe 15 or however long it takes.

MR. HIRSCH: It is my understanding the \$118 million that SMUD has in their budget is today's cost and the \$230 million to \$280 million that Mr. Clark said is today's cost. There is a little bit of disparity. I believe there is only \$38 million that has been put away.

ASSEMBLYMAN CONNELLY: My answer to that is the highest figure is too low. That's my experience with this. I bet my car on that too. I don't bet my car too often. Excuse me, Gwen.

CHAIRWOMAN MOORE: Since no one knows, and I think we will hear a little bit about that from the NRC or from some of the others. Until someone really knows decommissioning and that kind of thing, I guess, the cost -- Mr. Connelly is probably is correct -- maybe both of them are too low. I don't know.

The last question centers around the whole idea of the possibility of repowering. Is there any position that your group would take on the repowering of Rancho Seco as a gas fired facility?

MR. HIRSCH: We would have at this time no position, because we do not have enough information. We would certainly be

of interested. You have a lot of equipment and assets at Rancho Seco that has some value. If those can be converted, then it certainly should be looked at. You have other complications that we recognize when you do that which has been addressed by Mr. Latham. That's the air quality. But, at this time, I don't think there is enough information for us to make an evaluation.

CHAIRWOMAN MOORE: I shouldn't have said that was the last question, because it wasn't. This is. Does SAFE support PG&E's proposal?

MR. HIRSCH: No, we have no position at this time.

MR. GREG COOK: Thank you Madam Chairwoman. I am Greg Cook, the senior public affairs officer with the Nuclear Regulatory Commission based in Walnut Creek, California.

I have been asked to give you a little bit of a background on Rancho from an NRC perspective. I'm going to talk briefly about what the current shutdown of the plant means and why it occurs. What SMUD has to do to restart the facility and, I suppose from hearing that, some sort of judgment on how they are doing in that effort.

Also with me today is Martin G. Malsch, Deputy General Counsel for regulation and licensing, who is prepared to give you some information on decommissioning.

CHAIRWOMAN MOORE: Would you like to have him join you at the table. Mr. Malsch?

MR. COOK: To give you some background very briefly, the NRC mandate is to license and regulate the civilian use of radioactive material so that we can achieve a reasonable assurance of public and environmental safety. Without belaboring the long history and the litany that we have heard of minimum commitments and the desire to do no more than what was absolutely required, let me say, that over time, particularly with events in the early and mid-80's leading up to and culminating in the December 26 loss of integrated control system power event at Rancho Seco, NRC as an entity lost confidence in the entire facility, in the total safety of the facility as a whole unit. But I have to point out in saying that, that the safety systems in that facility performed adequately over time. The history of the safety-related systems at Rancho Seco has not been notably different from most other powerplants in the country. Why then are they shut down? Well, they are shut down in recognition of their commitment to provide a cause of the December 16 event. By that we mean not the loose wiring connection that initiated the event, but the causes behind that complicated event when it occurred. More significantly, at this point that issue has been pretty well handled by now, to justify resuming operations of the facility, again we get back to our assurance about a reasonable concerns of safety.

This does indeed mean we did not have that reasonable assurance when the plant shut down. When the plant was in the

condition it was on December 26 or December 27, 1985, the day after the event, it does not mean that we saw any irresolvable problems with the facility. Fundamentally the plant can be a safe facility. To date reviews of the Babcock and Wilcox plants conducted by the owners group and reviews by NRC indicates that these plants in total are not significantly different in their overall level of safety than other power reactors of other models. Although the staff is still reviewing the owner's group proposals and review. But, there is nothing there that can't really be fixed, physically speaking.

CHAIRWOMAN MOORE: Let me ask you something, so we can kind of expedite your testimony. You have heard over and over this morning the \$20 million figure or the committed \$480 million that SMUD was spend in trying to get the plant back in shape, and I guess to do the training of their staff and things that are necessary, is that a plan that has been approved as adequate by NRC?

MR. COOK: I think I can answer that by continuing briefly.

CHAIRWOMAN MOORE: Okay.

MR. COOK: SMUD needs basically two things to satisfy us to restart the plant. One is the stable management team made up at least predominantly of SMUD personnel. They have reached a point now where the management team is predominantly SMUD personnel. We have reason to believe that level of stability is

coming. We have sort of an all-star situation. People have been brought in from a number of different entities and a number of different backgrounds, but they have not yet had an extensive period of time to work together. There is some jelling that still needs to occur, but it is coming along pretty well. The second main item is completion of an acceptable plant rework, if you will, and test program. There are a number of subcomponents to that effort, and we have been able to pin those down with SMUD in recent meetings.

CHAIRWOMAN MOORE: Is that where the \$20 million has been spent?

MR. COOK: That's where the money is going. The money is going into the restart effort. There are extensive system reworks being done.

CHAIRWOMAN MOORE: So it would be pretty difficult to stop spending at the rate that they are, since they have already made commitments and the work has already either been concluded or is in the process of being done? Is that an accurate statement?

MR. COOK: Well, presumably if you slow expenditures, you slow the restart effort proportionately. That's essentially correct. There is a restart plan there. We have been talking with them about their restart plan and the design of that plan from day one. They are reaching a point where the plan itself is virtually in its final form. Much of the work is complete. Much

of the testing still has to be done. There are specific areas where there is more work to be done than in others, but all in all at this point we are able to say we believe they have a well defined plan. They have a good grip on the remaining issues. There have been marks of improvement, very positive signs for future safe operations.

CHAIRWOMAN MOORE: Just give me a guess, I guess is what I'm asking for. Given all the things with testing, how long do you think before they would be able to restart? Keeping in mind that we all know that you're only guessing and that there is no way that anybody can hold them to this.

MR. COOK: Our concern is that the work and the test can be accomplished and accomplished properly. Their current schedule calls for restart of the plant in July with a phased power ascension program following. The best I can say at this point is that is not out of reach.

CHAIRWOMAN MOORE: They have begin at a much lower capacity and build up over time?

MR. COOK: That's right. That's both to allow for what's known as hot functional testing of equipment and to provide additional operating experience for the plant operators who have not worked in an operating unit there now for some time.

MR. HIRSCH: For clarification, did he mean full power in July?

CHAIRWOMAN MOORE: No.

MR. COOK: No, I said restart in January with a phased power ascension program is what their current schedule shows.

ASSEMBLYMAN CONNELLY: Do you have any independent judgment as to accuracy of that schedule? Do you anticipate that the plant will start up in January or do you have enough information?

MR. COOK: It depends on a number of factors. That's their schedule. We believe they can make that schedule. We also believe that it is an ambitious schedule, but not out of reach.

ASSEMBLYMAN LONGSHORE: Has their main problem in the past been a people problem?

CHAIRWOMAN MOORE: Is Mr. Firlit here? Thought you were going to get away didn't you? Why don't you come up for a minute, maybe you can help us.

ASSEMBLYMAN LONGSHORE: Could you answer the question?

MR. COOK: Has there been a people problem? Well, there has been a problem in management turnover. Historically the utility was very reliant on contractors for basic functions such as engineering: very heavily reliant on contractor assistance. Today, they are much more self-reliant. They still use contractors. We certainly don't want to see them run all the contractors offsite, because you want outside expertise, but you also want to have enough capability to know whether or not your contractors are on track. We did see that level of expertise onsite today.

ASSEMBLYMAN LONGSHORE: Their main problem basically in the past have been people problems?

MR. COOK: Well, yes, I guess if you define the people problem in terms of organizational difficulty. Yes, there have been. There have been individuals who have been involved in the efforts since December 26 who may not have had the experience in the industry that the current staff has. That difference in experience and capability shows.

ASSEMBLYMAN LONGSHORE: Have you been satisfied with the training at all levels?

MR. COOK: We still have some training review going on, but their training program is much improved.

ASSEMBLYMAN LONGSHORE: Lower levels as well as the upper levels?

MR. COOK: Yes.

CHAIRWOMAN MOORE: Why don't we go to Mr. Firlit. I let you escape earlier and didn't mean to. You're the expert from the Nuclear Power Production for SMUD and you're the manager, so you can tell us about the plan. Does it look like it is going to start when it suppose to?

MR. JOE FIRLIT: Right now our plans call for our plant to heat up on December 5. That is where we leave cold shut down, the term that we use, at 210 degrees. We start heating our plant up to the normal operating temperatures and pressures of 534 degrees fahrenheit. We do all the hot functional testing that

Mr. Cook referred to. Then about the third week of January, we will start the reactor up and that's where you get the reactivity in the reactor itself. Then about the fourth week of January, we intend to start generating megawatts out of our plant and synchronize to the transmission lines and start producing power for the Sacramento district. Right now everything we are doing in terms of the outage is on schedule. We had a very intensive program that we had to put forth. We made a lot of modifications to our plant. In fact, we identified with the NRC probably over 415, I think was the number. To date, we have installed about 376 of those modifications before restart, and we intend to make the other modification changes before we restart our plant.

CHAIRWOMAN MOORE: How practical is it to have you to slow down the expenditures? You heard that being kicked around. Is it possible to do, given the manner in which the money is being used? I would think it would be difficult to do.

MR. FIRLIT: It would be very difficult to slow the plant down at this point of time, because you have the momentum of everybody onsite working to put the plant on line. The attitude of the people out there is very positive. They see the light at the end of the tunnel now, because they realize the plant is reality. It can be put on line in the time frame that we said it can. If you slow the plant down, it's not a one for one proposition. You can't delay the plant a week and lose a week on the tail end. What will happen is that you will lose the

contractors and your staff if that happens. In order to bring the contractors back in, it takes more than a week to get them back in there.

CHAIRWOMAN MOORE: The people were talking about you spending at a level of \$20 million a month, and people say well, only spent \$10 million in October, what would that mean?

MR. FIRLIT: That would mean we would have to lay off some of the contractors. That means we would probably breach our contract. We would have to pay the penalties for the clauses we have breached those contracts.

ASSEMBLYMAN LONGSHORE: So, it would actually cost you more?

MR. FIRLIT: Yes, in the long run. If we were to start the plant, say, in March versus January, it would cost the district more to do that and the rates would be higher.

ASSEMBLYMAN CONNELLY: That's based on the assumption the policy decision is to continue operating the plant, it would cost you more. There is no doubt about that.

MR. FIRLIT: That's correct. That's the assumption I was going on sir.

ASSEMBLYMAN CONNELLY: Are you the new fellow? There are so many of them, I can't keep track of them.

MR. FIRLIT: He's the production manager.

ASSEMBLYMAN CONNELLY: You're not the new guy out at the plant, I haven't meet yet.

MR. FIRLIT: Carl Adognini is our chief executive officer. He wanted to be here today, but he is in Washington.

ASSEMBLYMAN CONNELLY: I'm just trying to keep track. I meet one. I get to know them, and then they are gone.

MR. FIRLIT: I have been here since May 14th. I came from the State of Michigan where I worked for a utility for 22 years and ran the Palisades Nuclear Powerplant for a period of 22 years.

ASSEMBLYMAN CONNELLY: If you have been here since May 14th, you are a long-term management employee.

CHAIRWOMAN MOORE: Tell me what events occurred that changed the plan as it is now?

MR. FIRLIT: There are two things that we're doing to investigate our plan very thoroughly. With all the plants in the United States, I feel we have turned over every possible rock to find out what some of the problems have been in the past and what we might anticipate in the future. We are taking positive corrective steps to correct those problems. We're doing what we call an "expanded augmented system review and test program." Essentially what we do is we take a team of experts and they go out and look at 33 of our selected safety systems, and they review it from top to bottom. They look at the equipment. They look at the design. They look at the engineering calculations. They look at the procedures that we use to operate that plant, and they look for any discrepancies we may have. We committed to

the NRC that we would do all 33 systems. No other utility in the United States has done that yet. We have completed 18 of those. There is nothing we have found to date that has stopped us or will stop the restart. There is a risk that if something does come up that there is a safety deficiency out there, we would stop, fix that deficiency and that could delay start-up. That is a risk.

CHAIRWOMAN MOORE: You've only done 18 and that's over 21 months. You only got 3 months to finish that.

MR. FIRLIT: We started that program about 2 months ago.

CHAIRWOMAN MOORE: I see, so it is not something you have been doing over the whole period of time?

MR. FIRLIT: Right. Actually today we have about 24, but the report isn't written. When I said 18 have been completed, that means it has been thoroughly completed. The report has been written, and the report has been submitted to the NRC.

CHAIRWOMAN MOORE: What about the testing?

MR. FIRLIT: The test program is a very thorough test program that we're having. We are going through and identifying all the test requirements. We are looking at each component and testing it out separately. We are testing each system to make sure that the system itself works properly. Then we're doing what we call a plant integrated test program where we check that system against all the other systems and the interfaus. There,

again, since it is a very intensive test program, if there is any deficiencies that drop out of that test program, that is something we would have to correct, and that is something that could delay start-up. From my experience in test programs and the team that we have in place, I'm sure we can work around that aspect of it. I'm very confident we will have that plant on line in January of 1988.

CHAIRWOMAN MOORE: One of the real concerns that a lot of the people have is whether it will safety operate. You spoke of deficiencies and correcting them. How will you evaluate and check to be sure -- and when I say "you," I'm talking to Mr. Malsch and the NRC -- how will they satisfy you that these deficiencies have been corrected and the plant will be operating safety?

MR. COOK: We are reviewing both the system reviews and the test programs as they go along. We are evaluating the results of that effort as each system is completed. We will continue to follow through the test program in the same way.

CHAIRWOMAN MOORE: When they find a deficiency, where is NRC? Are you looking over their shoulders and seeing the deficiency and standing there to make sure it is corrected? Is that the way it works? Or, do they tell you "we had a deficiency and we corrected it?"

MR. COOK: Well, it's both in practical terms. We don't have enough people to be everywhere their people are. So, they

have a longstanding obligation as any licensee to tell us when they find a deficiency. We follow up with identification. Their definition of the deficiency and their corrective action. Now, sometimes we do find deficiencies on our own, but more often, in all honesty, deficiencies are found by the licensee and brought to our attention. Heaven help them if they find one and don't. That has not been a problem.

CHAIRWOMAN MOORE: In California we know a lot about efficiency.

MR. FIRLIT: If I can expand on Mr. Cook's comment at little bit. We understand the importance of having very good communications with the NRC and understand we have to keep them well informed. We meet with the region on a regular basis, at least once a month. We have met with the region people and the technical people out at the NRR in Washington as recently as September 16 on the overall comprehensive program we have in place. In fact that meeting went extremely well. Right now, we are scheduled to meet with five NRC commissioners in Washington on October 16 which is coming up shortly. This is the second key meeting we will have with the NRC commissioners. Barring anything that would stop up from starting our plant up in the last part of December or the first part of January, and at that time, assuming we have everything in place and all systems check out okay, and we have convinced the NRC that it is safe -- we will convince ourselves first and then we will convince the NRC

that it is safe to start our plant back up -- the NRC will vote at that particular time. It will take a majority vote, and there are five members on that commission.

CHAIRWOMAN MOORE: Are there any provisions or any plans to do any kind of public meetings so the public could be assured that all these things have been done, and that the public will have some input, the SAFE people while being opposed, they could be shown all these things have been met? There may be some positive benefits. Are there any plans by SMUD to do that before you turn it on?

MR. FIRLIT: We will be more than happy to do that. We tried to keep the people in Sacramento well informed. One a month before a board meeting, I hold a press conference.

ASSEMBLYMAN CONNELLY: Could I ask the representative from NRC a question? I know just generically for a second you were looking at the B and W plants as a whole. There was a petition filed by the Union of Concerned Scientists. I haven't been tracking it. Is the NRC is going to have hearings generally and so forth? Could you give a 30 second update on that?

MR. COOK: Yes. The Union of Concerned Scientists petition asked us to do several things. They asked to reassess the safety of Babcock and Wilcox plants in reference to technical issues. It asked to hold adjudicatory hearings to do that. It also asked us to issue an interim shutdown order until these hearings could be completed. That petition came in February.

The request for an interim shutdown order was denied. The response to the request for hearings on the technical issues is still pending from the staff.

ASSEMBLYMAN CONNELLY: So, we don't know yet whether there is going to be a hearing or not? In some respects it is almost irrelevant to what's happening in Sacramento, certainly on the short term, but in the long term it has implications? You mean on the broad issue?

MR. COOK: In the short term, you're correct. In the long term, it could have some implications. Yes. We don't know that yet. The staff's response has not been issued.

ASSEMBLYWOMAN CATHIE WRIGHT: The gentleman on the end, you are the legal counsel or just counsel?

MR. MALSH: Yes, I'm legal counsel for the commission.

ASSEMBLYWOMAN WRIGHT: Could you give us any idea what the decommissioning costs would be if that did take place?

MR. MALSH: Well, I'm not much of an expert on decommissioning cost. I have been working for some time on decommissioning rulemaking proceedings the commission has had under way for several years now. We have gotten hundreds of comments. The commission staff is just this month in the final stages of developing a final rulemaking recommendation to the commission. That would not only set up decommissioning options but also provide for acceptable means of funding decommissioning activities. What I have seen in the comments in terms of various

figures for decommissioning is something in the order of \$100 million. The difficulty has been how you define decommissioning. If you define it narrowly, including only removal of the radioactive contaminated components, that's one thing. Some people think it as also removing and demolishing the entire facility structures and returning it to its original state. That is considerably more expensive. So, while I am not an expert on what is a good figure, I do know enough from the comments one has to be careful in defining what is meant by decommissioning. That may be part of the source of the difficulty here. I'm not sure. Maybe Mr. Cook wants to mention something.

MR. COOK: The figure we submitted to Congress in April of this year was an estimate of \$130 million in 1986 dollars, counting only the removal of the radioactive materials and components in decontaminating the plant to the point that it could be release for unrestricted access from our perspective -- the radiological perspective. It didn't account at all for what a utility might be obligated to do to prevent people from entering into an abandoned building or any of the other issues that might be related. So typically, we hear those figures approximately doubled in order to account for the other activities the utility might have to undertake.

MR. FIRLIT: We agree very closely with Mr. Cook's figures. Our figure is here. I don't know if they handed this out to the members. There is a chart back there that talks about

the termination costs and decommissioning. Our overall costs for decommissioning, I assumes, is about \$213 million. That's in 1987 dollars.

ASSEMBLYMAN LONGSHORE: Your testing function is considered completely adequate to run safely as any other plant of its nature within the United States?

MR. FIRLIT: Yes.

ASSEMBLYMAN LONGSHORE: Barring some kind of internal sabotage and that sort of thing?

MR. FIRLIT: Well, all plants are subject to the same sort of sabotage issues. That doesn't change very much from site to site. This facility, assuming that we do permit restart -- and I think there is reason to assume that at this point -- this facility will have been reviewed, gone through and reworked to an extent that it would unequalled in the industry. There is every reason to expect that this will be certainly a safe and, in all probability, reliable facility.

ASSEMBLYMAN LONGSHORE: Thank you.

CHAIRWOMAN MOORE: Let me ask a couple of questions again to the NRC. You have heard some of the options that SMUD is faced with. Tell me what role will the NRC play if they indeed decided to transfer the operation to Duke? What will your role will be on some of the other options -- repowering option or the reconfiguration or any of those -- what role would you play? Give us some ideas along those lines.

MR. COOK: Let me give you some general background information on that. You know we have no actual proposals or papers before us. So, I couldn't prejudge what actually will occur in terms of our review. But I can tell you what the framework would be. As a general rule, no one can own and operate a nuclear powerplant without the commission's approval. No one can transfer their right to own and operate a plant either directly or indirectly without the commission's approval. Normally a transfer of operating rights or a transfer of ownership is accomplished by means of a request for a license amendment. That would be reviewed by the commission. They would have to submit whatever information the commission asked for to get the amendment approved. The focus would be on public health and safety. To a more limited extent, the protection of the common defense and security. The information you would expect to obtain in connection with the review would primarily focus on the technical qualifications of the prospective owner and operator: talking about management staffing, resources and things of that sort. Procedures are fairly straight-forward. They submit the license amendment. That is publicly available. There is in almost in all circumstances advance notice to the public officials of the state, advance public notification, staff review, and then eventual review and approval or disapproval of the license amendment. It's a fairly common occurrence for the staff to evaluate the license amendment request involving

ownership transfers. A little less common to review actual proposals, the transfer of operational responsibility, but the framework is there for doing those evaluations.

CHAIRWOMAN MOORE: Is there precedent for that some place?

MR. COOK: We have done that more in connection with financial restructuring of organizations than we have had large buyouts of utility operations. Recently there have been restructuring in which operational responsibilities are transferred to a different corporation under the control of some parent company. We have some experiences in dealing with those.

CHAIRWOMAN MOORE: But never for an entirely separate entity to take it over?

MR. COOK: I couldn't be certain about that. I wouldn't be surprised if that were the case.

CHAIRWOMAN MOORE: Are there any other questions? If not, let me thank you for your testimony. Let us move on the next panel which will be the panel on Resource Options and Transmissions Assess. If you all would come to the table then we can do that. Why don't we take no more than two minutes to make your initial comments? Just go down the line. PG&E, we already heard yours. SMUD, I think we pretty much heard from you in terms of what the options are. Why don't we hear from some of the offerors of the options? Why don't we start with Jerry Jordan?.

MR. JERRY JORDAN: Thank you, Madam Chairwoman, and members of the Committee. I'm Jerry Jordan. I'm Executive Director of the California Municipal Utilities Association. I'm here today appearing on behalf of the rest of the publicly-owned electric utilities in the state.

In our view the so-called consolidation offer from PG&E is nothing more than a hostile takeover attempt: a corporate raid, if you will. Designed primarily to eliminate PG&E's largest competitor in Northern California, and to take the focus away and provide a market for their past mismanagement and mistakes in overbuilding the nuclear powerplant in Diablo Canyon. This attempt is a characteristic predatory activity of PG&E. It is an anticompetitive practice, and it is viewed as such by the rest of the municipal utilities in the State of California. I have with me today two people to address that: Mr. Gordon White the manager of the Utilities Department in the City of Anaheim and past president of the California Municipal Utilities Association and the past president, also, of the American Public Power Association, along with Mike McDonald the general manager of the Northern California Power Agency. After they have briefly explained some of these anticompetitive practices, Madame Chairwoman, I'd like to have a few minutes to go over about six legislative proposals that we would make to the committee.

CHAIRWOMAN MOORE: We would like to hear that. I guess it is safe to say, you don't like the proposal.

MR. JORDAN: That's pretty safe to say. Yes.

CHAIRWOMAN MOORE: Okay. Let's go to your representatives.

MR. GORDON HOYT: My name is Gordon Hoyt, Madame Chairwoman. I am the General Manager of the Public Utilities Department for the City of Anaheim in California. I am a former president of the California Municipal Utilities Association and I am a past president of the American Public Power Association. The purpose of my testimony is to describe the importance of competition between investor-owned utilities, such as Pacific Gas & Electric Company and publicly-owned systems such as SMUD. How as a result of that competition California has a more economic and reliable electric power supply. The electric utility industry in this country is controlled to a great extent by large investor-owned utilities such as PG&E and Southern Cal Edison Company. There are only about 200 of these utilities operating today. These companies have vast generating and transmission resources. In contrast, the publicly-owned utilities generally are much smaller than the private utilities and many have no generating capacity of their own. The total generating capacity of the municipally-owned utilities is only a small fraction of the private companies. Despite having much more limited resources, consumer-owned electric systems play an important competitive role in the industry. They provide a competitive yardstick against which the performance of the private monopolies

can be measured, and force the private companies to operate more efficiency and economically.

Why are the private utilities constantly looking over their shoulders at the performance of their neighboring publics? The reason is simple. Public utility regulators are able to use the performance of publicly-owned utilities to help determine the legitimacy of rate increases sought by the private companies. Even more importantly, however, private utilities know that a viable public sector gives their ratepayers the real alternative to which to turn when private utilities' performance is inadequate. Despite low blocks thrown out by the privately-owned companies, publicly-owned utilities have made a tremendous contribution towards assuring a reliable and economical supply of power to the people of California by investing in generating resources, transmission facilities and seeking out new sources of economic power. The benefits of competitive pressure works both directions. The existence of publicly-owned systems as visible alternatives encourages private companies to operate more efficiently and attempt to hold down their rates. At the same time, the need to compete as effectively as private utilities has compelled the publicly-owned systems to devote their innovative skills and resources, both human and economic, to acquiring the power supplies at the lowest possible cost. The beneficiaries of the competitive tension between publicly- and privately-owned systems have been all of the customers of both kinds of systems

and all customers will suffer if that competition is diminished. That is a quick summary of my testimony of which I hope you get a chance to read.

CHAIRWOMAN MOORE: You weren't really reading. I wanted the people to know that. I saw your full testimony, which is much longer. Dr. Jan Hamrin.

MR. MICHAEL MCDONALD: Thank you Madam Chairwoman. My name is Michael McDonald. I'm the general manager of the Northern California Power Agency, which is a joint action agency of all 11 cities in Northern California that own an electric system along with one co-op, the Turlock Irrigation District. So, we view this proposed acquisition of SMUD by PG&E from the perspective of public power. I share all of the comments that Mr. Hoyt indicated. I share the comments in your opening remarks regarding the importance of public power to provide some measure of competition in the electric industry. I just wanted to make a couple of brief comments about some of the impacts that we feel would result for public power if this were to go through. We have filed written comments, which I certainly won't read, but I'd like to just hit on a couple of keypoints.

First of all, competition. The public power entity is almost by definition small and isolated. We have found it necessary in order to survive, in order to provide any kind of competition to band together and form cooperative arrangements where we can. NCPA is one of the examples itself, one of the

organizations we formed back in 1968. We, SMUD and other utilities have likewise pursued numbers of similar joint arrangements and partnerships. You have heard today about the project that SMUD is involved in to build a couple of geothermal plants, with a couple of other public entities. You have also heard about the Transmission Agency of Northern California pursuing the third AC line. There is another project that we're involved with SMUD called the Geysers Public Power Line, to build a line out of the geysers. Another very promising partnership is something called the Northern California Power Pool in which SMUD and NCPA and several other utilities are involved which would create a power pool for the public utilities in Northern California to do resource planning together, to pursue projects together and so forth. It has a lot of potential. The point I want to make is each of these joint ventures in which SMUD is involved would definitely be hampered, diminished. Their viability would be lessened if SMUD is no longer in the picture. That in turn means public power in Northern California would be that much less able to compete. I think it is pretty clear that the loser in that, equation is going to be the consumer in the final analysis.

I wanted to touch very quickly on transmission also, because you have heard SMUD indicate that they have a number of options that could solve some of their problems, but that transmission is the key to those solutions. They don't always have adequate

transmission to get the resource to their load. I just wanted to indicate that our organization has really been one where has been a history of that kind of struggle with PG&E. We do know they do not own their own transmission

linkages and networks. That's certainly the case with us. We have to rely on PG&E, and it has been a struggle from the day NCTA was formed. The question isn't often one of whether capacity is available. Many times capacity is available, there is simply an unwillingness on the part of PG&E to make it available under any kind of reasonable terms. Even our circumstance when we have an innerconnection agreement with PG&E that spells out the process by which additional capacity is built at our expense if its not there to begin with, we find obstacles and things thrown in our way to keep us from getting that which is contractually an obligation on the part of PG&E.

In our written testimony we have a number of examples that elaborate on that point. There is one, though, that is extremely illustrative that I think that bears mentioning in particular. I mentioned a second ago the Geysers Public Power Line which is aproject coming out of the Geysers. NCTA's participation in that line is a condition of our innerconnection agreement with PG&E. We have two plants in the Geysers. The transmission for the second plant is handled on an interim basis with PG&E, subject to us building the second line by a date certain, at which time the interim arrangement will terminate.

We have that obligation, and we are pursuing that through the licensing phase. We find it absolutely amazing that at the California Energy Commission, where we are going to obtain the license, one of the chief adversaries is PG&E, who is taking the position in front of the CEC that that line is not needed. That they have adequate capacity, notwithstanding the fact, they will not the relieve us of our obligation to build the line. Therefore, won't let us off the hook. If the line doesn't get built, they told us failure to obtain a license is not their concern. We have to have it built within a certain period of time or we will lose the transmission from our existing plant. In our efforts to negotiate with them a reasonable transmission agreement for the capacity that they testified is available, they terminate all negotiations. We find this to be extremely perplexing, but also fairly representative of the kinds of problems public power has.

CHAIRWOMAN MOORE: Didn't you hear Mr. Golub tell me earlier that third line was going to be built. There was really no need to look at that. PG&E? Because there were other options available in terms of transmission.

MR. MCDONALD: That's a different third line. What I'm talking about is the one coming out of the Geysers. The one he referred to is a third AC line up to the California/Oregon border. I agree that line will be built. It is unfortunate that the existing AC line couldn't be expanded. I think that would

have eliminated the necessity of a third AC line and it would have cost everybody a lot less money if it had of been approached that way. But again, we have written comments and in the interest of time, I'll stop there and respond to your questions.

CHAIRWOMAN MOORE: Okay.

MR. JORDAN: Madam Chairwoman, to deal with some of the problems that we're facing, we suggest the committee consider legislation in the following area. One of the problems that we face in a take-over attempt from a hostile corporation such as PG&E, is that the corporation can legally spend money trying to influence ballot initiatives. Public agencies can not. We would suggest that the Legislature consider disallowing the expenditures of funds by PG&E in order to influence voters and put them on an equal level, playing field if you will, with public agencies. The second proposal is perhaps the Attorney General should be requested or required, if that's possible, to engage in sort of an antitrust review. Looking at the anticompetitive practices in these take-overs. Third proposal is the PUC should be prohibited from allowing the cost of decommissioning to paid for by current PG&E ratepayers who are not in this area. I think that is a basic protection that ought to be given to those ratepayers if PG&E is going to buy a nuclear facility for the sole purpose of decommissioning it. We also think the PUC should be directed to prohibit geographical subsidies for rates. There is no reason why one geographical

area ought to subsidize another geographical area. If in fact there is going to be that kind of subsidy and if the rates are going to be frozen, then the PUC should probably be directed to make sure that it is the investors of PG&E, not the current ratepayers and not the future ratepayers, that pay for the cost of the freeze. Otherwise, it is not a real freeze.

CHAIRWOMAN MOORE: You are generating lots of questions.

MR. JORDAN: I know. I have just one more and I will be glad to take those questions. The last one is wheeling. That has been referred to here. Perhaps the solution is to require that if PG&E or any other investor-owned utility refuses or say they do not have the capacity to will, we and the small power producers be allowed access to their transmission facilities and to upgrade them at our expenses so that adequate capacity could be supplied.

CHAIRWOMAN MOORE: Mrs. Wright?

ASSEMBLYWOMAN WRIGHT: The first question for your associations that are represented here if you are so strong and so supportive of basically public-run as compared to the private, why weren't you on board to aid and help your friend in need, SMUD, when they started running into these problems? Were any of you there to assist or give advice? I mean your association, isn't your association there to help your fellow members?

MR. JORDAN: I think we are there morally. We're there with whatever technical support we have available. City of

Anaheim's utility is about fourth of a size of SMUD's. Our nuclear expertise is zero. We do own 3% of San Onofre Generating Station Unit 2 and 3, but we are not operators of the plant. We really don't have any expertise in the Rancho Seco area, if that's the area that you are thinking of.

ASSEMBLYWOMAN WRIGHT: I'm just thinking in general terms, because I'm not as familiar probably with what's going on in Northern California as I would be in Southern California because that's my home base, but certainly you have an association that is made up of small companies, it seems to me you have failed in what your real purpose is, and that is to aid and assist one another. My first question and then to Jerry, as much as I disfavor additional legislation, I interested because I'm looking at the last page of the statement where you have listed six areas which I assume -- those are the six areas where you're talking about legislation. So, I would ask you where is it in law now which would prevent the Public Utilities Commission from your own regulation, in regards to where they would prohibit or not prohibit decommissioning of Rancho Seco, the subsidies you talked about in 4, and the again subsidies in your item 5, or any of these areas where you have the PUC involved? If every little issue that comes up we are going to legislate to the PUC how they are to handle it, I think you take away the effectiveness of the PUC completely. Why don't we just abolish it and run the whole system through the Legislature?

CHAIRWOMAN MOORE: Before you go, let's go back up so Mrs. Wright's questions could be answered.

ASSEMBLYWOMAN WRIGHT: My first one why as an association so many of these public companies were not able to come forward and help? You have an association. Basically one of the reasons they are an association is to help and assist one another.

CHAIRWOMAN MOORE: It's like you asking why didn't one city in the League of Cities bail out another city with that city's taxes or whatever?

ASSEMBLYWOMAN WRIGHT: I'm not talking about funding mechanisms. I'm talking about they have the problem. They ended up with the financial problem, but starting out: with the difficulties they were running into, it seems to me there should of been enough expertise within the association. I'm just questioning that.

CHAIRWOMAN MOORE: It's the same thing. I just related to you the League of Cities.

ASSEMBLYWOMAN WRIGHT: The League of Cities is a little different situation.

CHAIRWOMAN MOORE: It's the same thing. It is exactly the same thing.

MR. JORDAN: In fact most of our members happen to be cities. The answeris, however, that we have been doing that. The stuff that Mr. McDonald was referring to is in fact that kind

of aid. We have banded together in joint power agencies and in joint projects in trying to get independence from PG&E and in particular independence from their transmission system. That is why in fact the California/Oregon Transmission Project which is the third AC innertie was started. It was only in Congress; that was going to be a project entirely public-owned. We did not seek any participation from investor-owned utilities. It was in Congress that the investor-owned utilities came in and sought to have a share of that line proportionate to the percentage of the load they served despite of the fact they controlled the transmission that exist already. We're forced in authorizing legislation from Congress, to be partners in that project. Frankly, at least from my own point of view, I question whether or not PG&E would really like to see that transmission project completed. But we are working together in various way to try to help each other out, and primarily in sharing the cost of building facilities we could not build individually on our own.

The answer to your second question, of course, is that the PUC if they choose to, could pass these regulations. The reason for the proposal, quite frankly, is that I question how interested PG&E would be in taking over the SMUD service territory, if these controls where in law. If in fact it was going to end up being a cost on their investors rather than future SMUD ratepayers or current or future PG&E ratepayers, I question if they would be interested in this take-over as they profess to be now.

ASSEMBLYWOMAN WRIGHT: One of my questions would be later on -- in fact I will make a statement and let you answer or whoever wish to. But from listening, I get the impression that maybe PG&E is supportive of the closing of Rancho Seco because they feel that is where the votes are in regards to the population here in Sacramento. That is what I think I'm hearing. I'm not sure. And, if that's the reason, and since it has been over 40 years in the battle between PG&E and SMUD, that probably PG&E sees the opportunity for take-over, and they talk around the bases of what they feel the public mood is in regards to the peer power.

CHAIRWOMAN MOORE: I don't think anybody will argue with that. I will hold Jerry hostage here and then you will get your shot.

You have described in all your comments and effectively so, a hostile take-over. I was going to ask you why you consider it a hostile take-over?

MR. JORDAN: Basically, because of the way it is being done. PG&E has already hired political consultants to convince the community that this is a good idea. They submitted the proposal in response to a request for power supply proposals. The way they have blitzed the Sacramento media and the meetings they are having with the Chamber of Commerce people and everybody else in Sacramento, just does not function in the realm of a friendly little negotiation. The fact they are pressing so hard

for these negotiations to begin prior to the time they make their bonafide offer. They don't have an offer on the table. They have, in fact, a letter saying that it might be a nice idea. They haven't offered SMUD any particular amount of money to do this. I think this looks exactly like a hostile take-over. That's in fact what it is.

CHAIRWOMAN MOORE: Okay. Mr. Longshore.

ASSEMBLYMAN LONGSHORE: Do you know if they have put any money into the initiative?

MR. JORDAN: I do not know that. I do know they were asked by members of the nuclear industry to put money in on the other side, and have not done that.

CHAIRWOMAN MOORE: Let's go to Dr. Hamrin.

MS. JAN HAMRIN: Thank you. I will be brief. I have three points I'd like to make. This all has to do with this topic which seems popular this morning on competition.

Our industry, and that is the industry of companies that build generating facilities from a variety of different technology and fuel types, has responded to the request for proposals from SMUD. And, is willing and able to provide a large variety of electric generation. Some of it baseload, some of it not, some dispatchable, some less dispatchable from a variety of different fuels. We did encourage our industry to respond. They have responded. We have had a problem; there hasn't been much happening since then. One question is how serious this RFP was,

where it was written, in my view, not as an actual substitute for Rancho Seco, it was for supplemental power for SMUD, in addition to the possibility of meeting power to replace Rancho Seco if it weren't brought on line. There are a lot of responses out there and they are very interested in the opportunity to sell their power at a competitive price. So, I think there is a need to move ahead on this and to give some indication back to those who have responded to the RFP as to whether in fact SMUD is interested in acting on any of those proposals. Where they are going. Right now, everything seems to be on hold. Certainly the PG&E issue has overshadowed...

CHAIRWOMAN MOORE: I think we heard SMUD earlier say they were going to begin evaluation of those proposals. I think Mr. Latham said they are going to begin evaluating those proposals in their future board meetings. Is that a fair statement?

MR. LATHAM: That's absolutely correct.

MS. HAMRIN: Good. The companies themselves have been told that a couple of times and nothing yet has happened.

CHAIRWOMAN MOORE: You just wanted it on the record.

MS. HAMRIN: I just wanted it on the record. The second issue is certainly the one of wheeling. I think it always keeps coming back to the fact that resources are not necessarily distributed in exactly the same way as the population in demand that uses electricity and that we frequently have more resources

for generating electricity located in one geographical area and the people who are using the electricity are some place else. I think particularly in the area of wholesale wheeling -- that's wheeling from those who are generating, to the utility that wants to purchase -- that there is definitely room for the state to move in facilitating that. I think suggestions that were just made about access to upgrading the system, if it were in need of upgrading, in order to take additional power is an interesting one. I think I suggest that maybe the burden of proof on this point should be on the company that says they don't have sufficient transmission in order to wheel, because this is a major problem of just having data in order to verify what the real situation is with regard to transmission. But I think getting the power from where it can be generated from the resources to the people who want to use it and whether that's a private utility or a public utility. The same thing holds true. We may have a situation where San Diego Gas and Electric will need additional power in the next year or two and not have the resources right in their immediate vicinity.

The third point I would like to make is one about standard offer contracts. Again, I think that an RFP went out from SMUD on a rather emergency-type basis trying to get a response back from people who are unclear about how contracts can be handled, whether the price that would be paid was short term, long term, whether it would escalate with inflation or with fuel

prices, and what would happen, and there hasn't been a lot of response coming back. I think in all cases, not just in investor-owned utilities but in public utilities such as SMUD that working out a process for handling contracts with independent producers, having standard contracts, having a database, having done the calculations of what your real marginal cost is, what it is you are shooting at and then whether you go into a bidding, competitive bidding type of process or something else, that would mean you would have the mechanisms there. So, if an emergency developed such as this or you are just anticipating future needs, you would know. You would have some idea what resources are out there. You would have some idea how you would handle contracting with them should you desire to do so. You would have the fundamental information in hand. I think that would be something very beneficial. Thank you.

CHAIRWOMAN MOORE: Thank you for your comments. Going right now the line. David Coleman?

MR. DAVID COLEMAN: Madam Chairwoman and members of the Assembly, my name is Dave Coleman. I'm the area manager for the Western Area Power Administration. Western serves wholesale power throughout the western 15 states. We have 5 area offices which covers regional areas. There are 2 area offices who serve California. My office, the Sacramento office, serves in northern, two-thirds of California and the northern two-thirds of Nevada.

In the interest of time I would just like to hit on a couple of highlights. You have a printed statement there from us. We have generating capacity in the Central Valley Project, hydroelectric, of about 1800 megawatts. Plus a 400 megawatt entitlement from the Pacific Northwest/Southwest innertie. Approximately 1400 megawatts of power are sold to 80 preference customers in California and Western Nevada. Surplus power is sold as it becomes accessible either through generation or imports at the time through PG&E. Our two largest customers are SMUD and PG&E. The federal government has been providing this cost-based wholesale power to preference customers in northern and central California since in the early 1950s. SMUD first became a customer in 1952. They currently have an entitlement of 360 megawatts; that has been mentioned earlier. What happens to the 360 megawatts if there is a consolidation? As with any of the contracts Western has with its preference customers, SMUD's contract with Western can not be assigned to any other party without Western's written approval. This approval for assignment cannot be granted if it results in violation of the Reclamation law. Western will carefully review any consolidation between SMUD and PG&E to see if it complies with the Reclamation law. If it should not under a merger a consolidation, the federal government will then withdraw the 360 megawatts and make a determination at that time as far what would happen to it.

I have additional comments regarding the COTP and some of the other transmission projects. I think in the interest of brevity, I'll stop at this point.

CHAIRWOMAN MOORE: Mr. Frizzelle?

ASSEMBLYMAN FRIZZELLE: If there is a consolidation, does the PUC regulate or not regulate?

MR. COLEMAN: Well, I'm representing the federal government.

ASSEMBLYMAN FRIZZELLE: I understand, but in this circumstance, I'm concerned regarding -- we had a lot of talk on competition of one kind or another. We have a concern in SMUD where electricity is furnished at a fairly reliable, lower rate than many. But, maybe that has something to do with the fact the PUC is regulating. The feds end up regulating, I presume, under some circumstances. Is that correct? When you use a nuclear facility, then the feds ends up regulating. Right?

MR. COLEMAN: That's through the Nuclear Regulatory Commission. I'm not prepared to speak to that.

ASSEMBLYMAN FRIZZELLE: It doesn't have anything to do with rates?

MR. COLEMAN: Well, our rates are involved through our Secretary's office and do get involved with FERC. So, from a rate standpoint, sir, actually from an allocation process, that would go up to the Secretary.

CHAIRWOMAN MOORE: NRC would regulate only for safety, not the rates. But if there were a consolidation, PG&E is still regulated by the PUC. The PUC would do the regulation.

ASSEMBLYMAN FRIZZELLE: I would think that would be a significant factor in the determination as to whether or not the public would want consolidation. If we end up with the PUC regulating and the ratebase set by the PUC, it could be varied from time to time by the PUC regardless. Whereas if the feds are basically regulating the power source and not only nuclear -- do you get into hydroelectric?

MR. COLEMAN: Yes sir. Actually ours is principally hydroelectric and coal fired steam.

ASSEMBLYMAN FRIZZELLE: So those kinds of things are fairly low rate circumstances and end up making...

CHAIRWOMAN MOORE: You're question is if there is consolidation, I guess, what would Western Power's role be with the new facility?

ASSEMBLYMAN FRIZZELLE: Yes, and the public ought to understand that. There is apparently a different criteria for rates.

MR. COLEMAN: The relationship towards the 360 would not change. But whether it remains with SMUD would be determined if they are still our preference customer under the law.

CHAIRWOMAN MOORE: Which they would not be if they were owned...

MR. COLEMAN: If they are owned -- if it is somehow situated with a for-profit company, and if what's remaining of SMUD is related to PG&E in terms of profit and loss.

CHAIRWOMAN MOORE: We didn't talk about that today, but basically under your proposal, SMUD would not continue to exist. Is that correct?

MR. GOLUB: Actually, that has not been flashed out. That is the kind of thing you needed to discuss.

ASSEMBLYMAN FRIZZELLE: That flashing out has to happen before the public makes a decision as to what they want.

MR. GOLUB: Yes, it would have to be before the public could decide. We agree. Now, when we had made our proposal, Mr. Jordan turned around and said, you didn't put a hard proposal on the table. That's a hostile take-over. We did it the other way, let's get together and and see if we can work out a proposal that seems reasonable and then present it to the voters.

CHAIRWOMAN MOORE: Wait a minute.

ASSEMBLYMAN FRIZZELLE: Even if you did that and even if you had a rate structure that you thought you could live with for a projected period of time, that does not have any binding effect on the PUC.

MR. GOLUB: No, you would have to make it subject to the PUC approval of those aspects such as the rate freeze.

CHAIRWOMAN MOORE: Wait a minute. We are jumping all over the board here. Let's kind of stay where you are. I think

Mr. Frizzelle is trying to get an answer to is what happens in this relationship? Your proposal is on the table now. I don't understand your comment about you don't know what happens to SMUD in that instance. If you're saying you are going to buyout and close down Rancho Seco, you are going to assume their liability and their debts, I would assume you are taking over everything that was SMUD as we know it and SMUD would no longer be around.

MR. GOLUB: It would not be operating as a utility, but I thought you were driving at a legal question that Mr. Coleman was dealing with which is you keep that legal structure and what does that mean?

CHAIRWOMAN MOORE: I think his expression is if there is no SMUD, there is no 360 megawatts. Is that essentially where you are coming from?

MR. COLEMAN: That's true.

ASSEMBLYMAN FRIZZELLE: This is the cutting point in which the public actually have to have significant input not just to what the rate structure as you propose it, but who is going to regulate the rate structure? Is it subject to variation due to other elements they do not have control over?

MR. GOLUB: When you get down to the stage on which the public actually votes on the matter, you would have to have a very specific idea in mind, I imagine, or least some plan they can deal with. And, yes, if it was subject to PUC review on the freeze, which it would be, you have to protect them by saying if

that doesn't materialize, you unwind the transaction or immediately get some views from the PUC while the process is moving forward. But as I say that's the kind of process -- investor-owned public utilities in this state are regulated. We do have to comply with the PUC requirements. The municipal utilities are regulated except we have more burdens in that sense. Yes.

CHAIRWOMAN MOORE: All right. We are going to try to keep moving along.

ASSEMBLYMAN LONGSHORE: I have a question, if I may.

CHAIRWOMAN MOORE: On the point.

ASSEMBLYMAN LONGSHORE: Pretty much on the point. Yes. How many is the preferred customers do you have now? You have PG&E and SMUD. Which others are preferred?

MR. COLEMAN: We have about 85 preferred customers in the preference customer category. Then we are allowed sell surplus power, and that's the category PG&E falls into. We can serve the investor-owned utilities.

CHAIRWOMAN MOORE: Why don't you describe real briefly what preferred class of customer?

MR. COLEMAN: Okay. The preferred class was designated under the Reclamation law by Congress to single out those type of customers such as the nonprofit municipalities, irrigation districts, water districts, those kinds of loads. In California, for instance in this area, we have Roseville, beside SMUD, we

have the Air Force base and quite a few military installation, Palo Alto, Santa Clara, Redding, and many cities and irrigation districts from the Tehachapis north to the Oregon border we serve. For instance, Los Angeles Department of Water and Power is a public entity as opposed to Southern California Edison being an IOU, and you are acquainted with that. We can serve a preference customer that falls in that category as a nonprofit organization.

ASSEMBLYMAN LONGSHORE: And your rates are definitely lower to them?

MR. COLEMAN: As a general rule, they are, yes, because it is based on the hydro-system which is CAP and then some imports from the northwest.

ASSEMBLYMAN LONGSHORE: And the 360 they now enjoy is their portion, would that be redistributed or would it go to PG&E?

MR. COLEMAN: Right now, it is premature to make a statement. It might be redistributed. I don't know. We would have to go through a formal process with public hearings, and there is a regulated Administrative Procedures Act and a regular process we go through, sir.

ASSEMBLYMAN LONGSHORE: But without that, PG&E's cost would definitely be higher. Would they not?

MR. COLEMAN: It would be up to them to make that statement. I would think so, because of the low cost 360 megawatts coming from the federal government.

MR. GOLUB: We are seeking to see if we can work out arrangements that would concentrate the benefits of that power in the SMUD area after a consolidation. That's one of the things we're reviewing. Such as delivering the power to various public agencies within the area, government offices and things of that sort.

ASSEMBLYMAN LONGSHORE: (INAUDIBLE)

MR. GOLUB: The problem is that under the law we don't get a fair chance to buy it even if we want to pay more than the municipality. We are trying to preserve the benefit for the area, because we are trying to give the area an arrangement which is significantly better than the current situation they are facing. This would be a component of that.

CHAIRWOMAN MOORE: Mrs. Wright.

ASSEMBLYWOMAN WRIGHT: If you are trying to aid SMUD, giving them assistance basically, why would you not then set SMUD up as subsidiary company so it maintained...

MR. GOLUB: Well, first of all these gentlemen here would be the first to shout they don't like the idea of a public entity being a subsidiary of a investor-owned utility. But the real reason is that I don't know what you would gain by the bureaucracy that you would create. The two systems right now are really natural partners. We have the resources. We have the employees. The market in the Sacramento area is growing. It can spread the fixed cost of our system over more customers,

resulting in lower costs for everyone. I don't know what you would gain in the extra structure, but if it was something important, I suppose we could look at it.

ASSEMBLYWOMAN WRIGHT: I was thinking in terms of what you were discussing now about the way they are preferred customers and PG&E is a surplus.

MR. GOLUB: I'm sorry. When I earlier mentioned to the Chairwoman we hadn't really flashed out whether SMUD would continue as an organization, I was thinking of something similiar which was as an independent organization that somehow might serve this purpose rather than a formal subsidiary. We're trying to get away from the semantics. We are trying to get a business arrangement that results in the least cost, the best service. That's where we don't want to feel constrained by the kind of slogans that I'm hearing out of the past about who owns what and what's the structure. Let's find out something that gets the lowest costs, and give the people of this area the choice of deciding. The SMUD board people have just said to you that they want to look at our proposal. These people from other areas come in and say they don't like the investor-owned utilities.

CHAIRWOMAN MOORE: If I let you continue along these lines, you are going to continue my hearing 15 minutes. I going to have to let everybody come back and rebutt, and I'm not going to do that. So, you are not going to go along those lines. So, we are going to go to Mr. Wright and hear from the Bonneville Power Administration.

MR. STEVE WRIGHT: Thank you, Madame Chairwoman. My name is Steve Wright from the Bonneville Power Administration. I'm here representing Jim Jura, the administrator from Bonneville Power. I would like to thank you and particularly your staff for this invitation to appear today. To my knowledge, this is the first time Bonneville Power has appeared before a committee of the California Legislature.

BPA's primary responsibility, according to statute, is to serve the 4 state area of the pacific northwest: Montana, Idaho, Oregon and Washington. However, BPA is not, that has been referred in some cases, not a carpetbagger coming in trying to take advantage of the situation. We have a long-standing relationship with California utilities. Since the innertie was energized in 1968, 20 years ago, we have sold something like 350 million megawatt hours of power into the State of California. That has saved ratepayers both in northwest and California literally billions of dollars. We have relationships with all of the utilities represented here at this table, and in fact, all the utilities in the State of California.

We have made an offer to the Sacramento Municipal Utility District. That offer is based, we believe, on the strength we have in the bulk power supply market, and the constraints we are faced with. Let me spend a minute just describing the strengths to you.

We believe we are the low cost supplier in the bulk power supply market. We have made an offer to the Sacramento Municipal Utilities District of approximately 100 megawatts starting at about 30 mills per kilowatt hour, which is, as we understand it, is about 25% less than SMUD's alternative costs. We have significant surpluses in the northwest. We are prepared to sell on a 20-year basis. We believe we provide price predictability, and we have enough transmission to be able to deliver the power to the border. Given that, we have this great power to sell and the question you may have is why haven't we consummated a deal so far. Let me spend a second talking about the constraints that we have in that market.

First of all there are constraints in regards to transmission access in Northern California. We can deliver the power to the border. SMUD has approximately 200 megawatts of intertie capacity that would allow that power to be delivered from the border to the SMUD system. About 100 megawatts, as we understand it, is currently contractually committed. So, there is the remaining 100 megawatts. We believe we have enough power. We have made an offer, in fact, that extends up to about 725 megawatts of energy. Thirteen hundred and fifty megawatts of capacity. So, given additional transmission, we believe we could serve additional power to SMUD.

There are two other constraints that come into play as well as transmission. First is our legislative statutes that we

operate under, which requires that any power that we sell be surplus to the needs of the Northwest. So, in any contract that we offer to a California utility we have to be able to guarantee that the power will be excess to needs of the Northwest. This creates some concern for California utilities whether the power will be available 15 or 20 down the road.

Third, there is also concern about what is known as the single largest outage on the utility system. In effect, we have only one transmission line that goes into the SMUD system. If that transmission line goes out there will be problems in making sure the lights stay on, and there is a need for reserve. Given these strengths and constraints that we see in the system, we made a three part offer to SMUD that we believe will deal those constraints.

First we made an offer that would allow us to sell 100 megawatts of power to SMUD starting immediately. Whenever point SMUD is interested in starting it.

Second, given that the California/Oregon Transmission Project is on the board and it is apparent that it is going forward, we made an offer to sell additional power upon the completion of that line. It is our understanding that SMUD would have up to about 200 megawatts of capacity. Given the utilization of that line, we will be happy to sell an amount that would be consistent with that additional capacity.

Third, recognizing the constraints that we have and recognizing in some ways our system and PG&E's system are a real match, we have made an offer to SMUD and to PG&E to enter into a joint venture that would allow us and PG&E to make a larger sale to SMUD. It is our belief we do have a fair amount of low-cost power that could benefit the District's ratepayers. Given the constraints that we have it appears that we might be able to put together a deal where ratepayers of PG&E, the Northwest and SMUD could benefit. We have received a response from PG&E that indicates they would be willing to evaluate any proposals that we put forward. We do intend to go forward with such proposal and we hope to meet with them soon.

CHAIRWOMAN MOORE: You have not heard from SMUD?

MR. WRIGHT: We have heard from SMUD that they would be interested in seeing if we could find way to get power to their system. I will conclude my statement with that.

CHAIRWOMAN MOORE: We are going to move on to -- I haven't forgotten you. We will get back and having closing words from SMUD and PG&E. Let's move on to the customers' perspectives. Are there any questions of the members? Why don't we let PG&E and SMUD make their comments? Is there anything you want to add?

MR. FRANK HAHN: Yes. I would like to add one thing. I think if you refer the charts. My name is Frank Hahn. I'm Deputy General Manager of SMUD. I think one thing that is very

important to notice on the charts behind me, the top red line are PG&E rates that are forcasted in their submittals to the California Energy Commission. The bottom of that red area is if PG&E succeeded in getting what the PUC staff recommends goes into the rate base. The top line there, on top of the yellow band, that if SMUD would terminate Rancho Seco; walk away from it, and purchase power under a contractual arrangement that has been offered by PG&E in response to the request for proposal. It also assumes higher level of decommissioning costs. It also assumes some dry years take place. In every instance over the long term Sacramento rate customer owner is better off than PG&E ratepayer in future. What SMUD is looking at in options are shown in the green band. That includes the repowering. It includes the holding company. The bottom line includes the restart.

CHAIRWOMAN MOORE: The top yellow one is the worst case.

MR. HAHN: That worst case has been reviewed by independent consultants, by the Standard and Poore, by Moody's and by the investor bankers and it has been declared the worst case. It's like selling your house if you lived on the American River and indicating that Folsom Dam could break. That's the kind of worst case it is.

CHAIRWOMAN MOORE: Okay. The green represents....

MR. HAHN: Those are the options. All of the options we are looking at that have been described to you fall in that band.

CHAIRWOMAN MOORE: Of course, now, I'm going to have to let Mr. Golub go, and he is going to tell me how wrong that...

MR. HAHN: If you look at the next chart that's one interpretation of PG&E's offer that is behind you where rates are frozen for 3 years. You can see the immediate public appeal to that is the red line stays level. Unfortunately, that stays level for 3 years and it shows you that the ratepayers, under the proposal that would freeze the rates, do benefit in the short term. But in the long term, we don't.

CHAIRWOMAN MOORE: Now, see what you did? I have got to let Mr. Golub respond.

MR. GOLUB: I hadn't seen any of these charts until just now. I'm glad to see though that SMUD is approaching this with an open mind as they indicated they would. They came with these prepared charts. In any event, I can't really comment on that except to say that one there gives an assumption as to the length of the freeze and as to what ultimate rates will be and how fast it will escalate. All of the things that one would flush out. This chart, which I only saw when I sat down only a few moments ago, I spot an error in it right now that changes the whole thing.

As of today our rates are lower than the rate SMUD charges 53% of their customers. I have the actual rate figures. Our rates are basically right in the middle of their residential rate.

CHAIRWOMAN MOORE: Your proposal is to freeze their current rates, not yours, isn't it?

MR. GOLUB: We are proposing a rate freeze in that element of which one used -- we haven't gone through -- but the freeze at the minimum means no one's rates will go up.

CHAIRWOMAN MOORE: Wait, wait, wait. Are you telling me something that I didn't know before?

MR. GOLUB: Yes.

CHAIRWOMAN MOORE: Is there a possibility that what we think is the rate that is going to be frozen may not be the rate that's going to be frozen?

MR. GOLUB: It is going to be least as good as you think. I think the argument should even be better. But it would be at least as good, there will be no increase.

CHAIRWOMAN MOORE: First of all, as for SMUD, this is an all-time high for them. So to freeze it at that level is not what I would consider good. If your rate is considerably lower, obviously that would be one...

MR. GOLUB: Our rate is lower for homes with electric -- I can give you the numbers as to what they are. They are basically close, but our rates are lower. My point, though, when I look at this chart, which I have never seen before, you look at where the starting point, they start the PG&E line about a mill and a half higher than their line. I know that's inaccurate right this moment. I don't have to engage a consultant to tell

you that. If you move that base line down, and you move the red thing down proportionately, you will find that the red thing overlaps their green and yellow thing.

CHAIRWOMAN MOORE: The reasons why your rates are lower because you have baseline in it and that is one that they don't have.

MR. GOLUB: I think they have a small baseline. From a ratepayer perspective, as long as we are giving the ratepayer a good product...

CHAIRWOMAN MOORE: The general thought has been that when you talk in the past about freezing rates, it has been SMUD's rates you were talking about. So, I'm pleased to hear that you are not talking about SMUD rates.

MR. GOLUB: We are saying this. People in the SMUD area will have their rates at the least frozen and not increase over the rate freeze. You raised really a refined question, you said what if the PG&E rate is even lower than SMUD rates. We haven't gotten to that kind of a notion of a rollback. That's what I thought you were asking me.

CHAIRWOMAN MOORE: It is. It really is.

MR. GOLUB: We haven't gotten to that kind of refinement, but basically, certainly as to the basic freeze, we're there and unequivocally so. This chart is off right away because the base point is off. I can see it by looking at it. Obviously, you don't have the time to examine the details of it.

I'd like to know what's behind it. But right away I can tell the base is off at 1987. It is just wrong. We are at the same point in rates as they are. If you put those two side by side, then just looking at his chart, the two lines tend to overlap almost precisely if you start off at the same spot.

I also know a few other basic things that SMUD projects a 37% increase and I know that we do not project increase of that magnitude, despite even the most favorable outcome of the Diablo case, our projected increases will be less than half that. There is something wrong with that chart, but I can't give you the details because I just saw it today for the first time.

MR. HAHN: If I can just make a comment. Those are system average rates. Those are not rate structures. He is speaking to rate structures, and it is true that 50% of the residents are effected by this. But he doesn't tell you how much lower PG&E's rates are for the commerical and industrial customers because in fact SMUD are considerably lower than PG&E's.

CHAIRWOMAN MOORE: We're going to move on.

MR. GOLUB: Will I have a chance to address some of these other comments?

CHAIRWOMAN MOORE: We will give you 2 minutes to sum up your comments.

MR. GOLUB: I'll take less. We think the proposal should be evaluated on its merits and the benefits to the

consumers on both systems. We think the polemics about public power, which are essentially ideological, are irrelevant. As far as diversity as Northern California is concerned you have the Western Air Power Administration, the Bonneville Power Administration, 12 or so municipalities, several irrigation districts, all of that will be in the power business one way or the other regardless what will happen to the consolidation proposal. All of that goes forward. None of that would change.

CHAIRWOMAN MOORE: That means you are going to aggressively pursue the Bonneville Power offer in the same manner that you are pursuing the SMUD?

MR. GOLUB: We have already committed to work with and on that. Obviously, we want the arrangement that results in the least cost to our customers. We will work with them. If that proposal makes sense, we will pursue that one.

CHAIRWOMAN MOORE: On the surface, it sounds like it makes a lot of sense. All right. We are going to move on to the next panel.

ASSEMBLYMAN FRIZZELLE: While you're moving, I'd like to point out if PG&E, and I tend to favor private power rather than public power, if PG&E picks up the assets in this arrangement with SMUD, I presume you would also pick up such things as the hydroelectric facilities, the contracts regarding various sources of power, the 85 preferred customers so to speak areas which would broaden the scope of your customer base. Presumably then by

broadening and adding more customers and adding low power capital assets with the hydroelectric and so forth, you would probably end up with a lower cost factor than even you can project at the moment?

MR. GOLUB: Basically, that's correct. The natural fit of the two systems would result in lower costs for both our consumers and their consumers. So, it is a win-win kind of situation.

ASSEMBLYMAN FRIZZELLE: So, the kinds of things that would enable them to deliver at the rate structure that they are delivering, you would pick up as assets to your company which would most likely allow you to lower your rate structure as well?

MR. GOLUB: Basically, that's correct. But the main thing that causes the reduced rate is not so much their generating resources as the shape of their market. Because it is a growing market and we can spread the cost of the integrated system over to more people.

CHAIRWOMAN MOORE: Speaking of that, we didn't talk about it at all but with Diablo coming on line and the potential there, you talked about a 37% rate increase for SMUD, but with the spread of Diablo over there, we looking at how much? What would be the potential increase as they absorb some of the cost of Diablo?

MR. GOLUB: When I saw the chart, I searched in my memory for the number, but I know it less than half that. I don't have the precise number. I can supply that later.

CHAIRWOMAN MOORE: Why don't you do that. Why don't we go to our last panel who represents the ratepayers and the people who have to bear the brunt of any decisions that are really being made. Why don't we go right down the list. I have four people and three names. Why don't we start with the person who I don't have which is the young lady here? Tell me who you are?

MS. WENDY PRICE: I'm Dee Price, and I'm the founder and the current chairman of the SMUD Ratepayers Association. I will defer to Dennis Diede our vice president. But I do have a suggestion for some legislation.

MR. DENNIS DIEDE: Chairwoman Moore, I'm Dennis Diede, vice president of the SMUD Ratepayers Association. We have been studying the issue since PG&E first actually got involved in talking about buying SMUD. Since then we seen five or six options that have come up before the board of directors. We feel before a decision to sell SMUD is made that other alternatives need to be addressed and inherent problems must be solved. From our grassroots perspective, we see SMUD with several problems. The first being ineffective and unresponsive management. This occurs from top to bottom in SMUD. I personally have 20 years of experience dealing with SMUD from all levels from the board of directors to line crewmen, to welders, and ditch diggers in the street. This is an ineffective management at SMUD. This results in financial problems and that's what got SMUD into trouble. This management caused the problems at Rancho Seco when it was

originally built. These problems are now being addressed and paid for long after the people who did the original construction have gone down the road.

The next problem I'd like to address is the lack of public overview and its scrutiny. The board of directors gives the information before the board meetings, but this information comes out sporadically and is almost unintelligible because you cannot fit the different pieces together into a clear view of what's going on.

CHAIRWOMAN MOORE: Under law, we have directed SMUD provide a better public forum. Is that not occurring?

MR. DIEDE: Not to my knowledge. I have been having problems in getting information from SMUD. I would like to relay one of those to you. I was in SMUD's office on Thursday of last week. I went to the security officer and requested to talk to somebody who can give me the management structure chart of SMUD. He wouldn't let me go to any of the officers until he was on the phone 15 or 20 minutes trying to find the one person who can give me the information. When he failed, he finally sent me to the 3rd floor, to the Personnel Department. Fifteen minutes later the lady in the Personnel Department finally came up with a management structure that was almost 6 months old. It was a very poor copy at that. I would think that this information should be on the counter in SMUD's main office available to anybody who wants to walk into the door and pick it up. It took me another hour to

obtain a copy of the MUD Act and financial statements from SMUD. There again this information is only available if you know what to ask for and you are persistent enough to get to the right person who is willing to give it to you. We see this as a problem.

We see padded payrolls and favoritism in promotions, demotions, hirings, firings, and in the way job assignments are laid out. I have seen these things personally over the years.

Now, comes on the problem of Rancho Seco and it creates uncertainty and fear in the minds of the ratepayers. When there is still uncertainty they begin to say "Any way out, PG&E's offer looks real good." But they don't have all the information they need, because they get information out of news articles, they get it out of public broadcast, by SMUD, by PG&E, conflicting information, and we believe that has to be solved too.

CHAIRWOMAN MOORE: Let me see if I'm clear in your comments. You said a lot of things, but basically there is a tremendous need, as you see it and in your group, for the SMUD board to be more open to the public in the working out of the customers' concerns.

MR. DIEDE: If you would bear with me I have a few solutions that I would like to make recommendation to you.

First of all SMUD should adopt a policy of complete information and make it readably available; not fragments of information. Give the public access to records upon request

rather than having going through a security guard and fifteen other departments to get to the guy who got the information.

CHAIRWOMAN MOORE: When you say SMUD records, what do you mean?

MR. DIEDE: Financial records on how much they spent on line crew and chief salary in a year.

CHAIRWOMAN MOORE: You mean public information.

MR. DIEDE: It's like you have to know somebody who known somebody who knows somebody to get anything. That's not fair. The other thing is they hired a new manager. They now need to give him room to control, to reorganize, streamline and report facts to the public and to the board without individual board members screening what he says; changing the meaning of his words, and giving their own points of view different from his. If he is a good manager, let me manage. If he is not a good manager, terminate him. But the board should get out of the day-to-day operations of the manager's office.

CHAIRWOMAN MOORE: In defense of the board, on the one hand the people are attacking them for not doing very much of what they are supposed to do, and on the other hand you're saying that they should not be involved.

MR. DIEDE: We believe the board should set policies. The actual way the policy is implemented has got to be at the direction of that individual who was hired and has expertise in management. That's all we're getting at.

CHAIRWOMAN MOORE: There was a bill and that was supported by the SMUD board that did get very far in this Legislature which would have done just what you wanted it to do. It would allow the general manager to totally run the enterprise, but we feel that the SMUD board is accountable to the people who elect them.

MR. DIEDE: I don't mean to say that the manager shouldn't be accountable to the board, but to the board as a whole, not to an individual board member who shows up in its office on Friday afternoon and says, I want you to do this and I want you to do that.

CHAIRWOMAN MOORE: That's the responsibility of the board.

MR. DIEDE: We believe those things need to be considered.

CHAIRWOMAN MOORE: You want legislation to present someone on Friday afternoon.

MR. DIEDE: No, no. I'm saying the manager is torn apart by five directors in five different directions.

CHAIRWOMAN MOORE: Some thing we can not legislate.

MR. DIEDE: At least you allowed me speak it in the open and I appreciate that.

CHAIRWOMAN MOORE: Okay. Go ahead.

MR. DIEDE: Lastly, the more the taxpayers and ratepayers from our county know about SMUD, and the more open

SMUD is with their information, the more intelligent the decision they can make when it comes to the ballot. We hear a lot of frustration on the street. People say there is just no way to solve the problem, so sell it to somebody. Let's just get rid of it. We as the Ratepayers Association thinks there is a better way. Fix the problem, then we won't need to sell SMUD to PG&E.

CHAIRWOMAN MOORE: Are there public meetings being held giving the public general information about some of the things that are going on internally? Are they being done? Thursday night, is that done on a regular basis?

MR. DIEDE: SMUD board meetings are twice a month. We were thinking something more along the lines that SMUD acknowledge certain groups like SAFE and our Ratepayers Association and several others and direct press releases to them to keep them informed and allow us to inform our constituency if you will.

CHAIRWOMAN MOORE: So, you are not on the mailing list.

MR. DIEDE: We are not on a mailing list. You fall off the mailing list as the days go by. You don't know whether your are on or off.

CHAIRWOMAN MOORE: All right. Thank you.

MS. PRICE: Thank you. I will be brief. We have heard that they are spending \$20 million per month to repair Rancho Seco. That does not include the cost of purchasing outside power. At \$20 million a month for 12 months, that \$240 million.

That Thursday evening the board approved the sale of \$150 million worth of bonds. That is not going to cover one year. We also heard 37% rate increase in the next 18 months. That was SMUD's announcement. At last Thursday's board meeting, I was assured by the board and Mr. Frank Tindal that there would be no rate increase in the next 12 months. Does that mean we are going to be impacted with a 37% increase within a 6 month period? This organization has been long been a supporter of nuclear power; of Rancho Seco until we had good cause to criticize. We now feel that maybe it is going to take legislation to set up a public affairs, or public information office such as the California Energy Commission has, or the PUC has to assist ratepayers with getting through to the proper channels at SMUD. We constantly hear complaints from ratepayers. I have experienced some of them; customer service-type complaints.

ASSEMBLYWOMAN WRIGHT: If I may?

CHAIRWOMAN MOORE: Mrs. Wright.

ASSEMBLYWOMAN WRIGHT: I look upon the SMUD board the same as I would the City Counsel. I would ask you since they are the policy makers and what you are asking is for a policy decision. In the course of their meetings do they have a point in time when they take public input on any issue the public wishes to bring up?

MS. PRICE: Generally, under Statements From Visitors, which is at the end of meeting which could be midnight to 2 o'clock in the morning.

ASSEMBLYWOMAN WRIGHT: They usually have someone from city council that wants to listen to them.

MS. PRICE: Sometimes it after a specific controversial issue.

ASSEMBLYWOMAN WRIGHT: Have you suggested to the board that they have this public input in the beginning of the meetings. When do they start, 6:30, 7:30?

MS. PRICE: This was done in the past. This was changed immediately following TMI because we had a large number of anti-nuclear people coming and very frankly fillibustering and stretching the meetings out to 2 or 3 in the morning.

ASSEMBLYWOMAN WRIGHT: Again, the Chairman of that board has the right at that point to point-blank, upfront, tell you how long you're going to speak and what they are going to accept and not accept. They can control that as a public entity. They can control that. I just don't like legislation that constantly tells people how they are supposed to run their show. I really sincerely feel that the kind of information that I'm hearing from you should be directed at the board and they should be put on record as to how they are going to approach it or listen to what you have to say. Because they have to come up for reelection, correct?

MS. PRICE: That's right.

ASSEMBLYWOMAN WRIGHT: Yeah. You're the constituency. They either listen or they are out of a job.

MS. PRICE: I would like to respectfully suggest that this committee attend some SMUD board meetings and see how the public is treated. If we were treated like we are treated today at the SMUD board meetings, I don't think we would be having some of problems we are having right now.

ASSEMBLYWOMAN WRIGHT: When are they up for reelection?

MS. PRICE: November 1988, three of them.

ASSEMBLYWOMAN WRIGHT: Well, what are you going to do about it?

CHAIRWOMAN MOORE: We are going to record that Mrs. Wright moves everybody thrown out of office.

MS. PRICE: Can I make one point please?

CHAIRWOMAN MOORE: Sure.

MS. PRICE: We have gotten bits and pieces of nuclear operations budget, and I know of other individuals throughout this country have tried to get that information. It is literally impossible. I know there was a group that was going to go to court to get it. We have a fear and I wish that SMUD would prove us wrong. I wish they would stand up and make the information very public. But if you took the cost of construction for Rancho Seco and all of the repair cost, the nuclear maintenance or online modifications, that we have now put more into that plant than it is worth on paper. If SMUD board and staff can prove that we're wrong on that, we would be thrilled to death to hear it. But it means they are going to have to make public all budget for nuclear operations, and we would like to see it.

CHAIRWOMAN MOORE: I think the budget ought to be part of public information since public dollars are expended on it. I guess my question would be, so what?

MS. PRICE: Well, it becomes a time no matter how much you want to keep your old car, you just don't continue to put money into it if it is not economically feasible. And we really don't know if we are at that point or not.

CHAIRWOMAN MOORE: I think the question is that they are on the threshold of a restart, so to speak, and you said your group has been a supporter of nuclear power, we are three months away out of a \$20 million a month program, it doesn't seem to make much sense at this point to stop. You heard what it would mean to try to stop it. I'm just not so sure I agree with you. In terms of public information, you ought to know that. You ought to have those figures and shouldn't have to fight for it. I think the board members today that will hear the word and maybe that will help to free up that information.

ASSEMBLYWOMAN WRIGHT: Three votes are here, isn't it? We should be able to get something.

CHAIRWOMAN MOORE: What did you say a quorum? Mrs. Wright is saying the quorum is here. They can make your budget and stuff available.

ASSEMBLYMAN LONGSHORE: It would seem we're starting a new business or that would be the point of view that you should look at as far as Rancho Seco is concerned. If you curtail it or

stop it at this point you would never, ever have the opportunity to recover. Whereas if you continue with the 3 months, you do have the opportunity to recover your costs. So, in effect, what you're saying is everything they have spent at this point in time, we either trashcan or we take the opportunity for 3 months more of deciding as to whether or not we are going to be able to recover our costs. I think that should be the approach.

MRS. PRICE: That's true. It's three months now, and three years ago we were saying the same thing. We were getting the same amount of information that we have gotten to date.

ASSEMBLYMAN LONGSHORE: Today you have heard the federal government who testified. You have heard a number of other people testified that would probably bear witness to the fact that SMUD is on track this time.

CHAIRWOMAN MOORE: I guess that still doesn't really answer your question, but let's move on and hear from the business community, by Mr. Jim Butz. Then we will wind up with my friend Ed Lewis.

MR. JIM Butz: First of all I appreciate the opportunity to come out here from our headquarters in Pennsylvania.

CHAIRWOMAN MOORE: Why don't you identify yourself and speak right into the mike?

MR. Butz: My name is Jim Butz, and I'm the manager of Electric Supply, Air Products and Chemical Incorporated. I'm responsible for the purchase of \$180 million a year for

electricity in the United States at approximately 30 major facilities of our company. Twelve million dollars of that purchase occurs in Northern California at two locations: Santa Clara and SMUD. It is not an accident that those two locations in Northern California are on public power.

I might as well cut some of my testimony short given the time. You have not only my full text, but you also have an outline in front of you. Suffice it to say that my position is that I think a PG&E merger with SMUD would be a very grave mistake. Given the amount of money that my company spends with SMUD, which is \$6 million a year, I have taken a very careful look at all of SMUD's resource plans over the last 3 or 4 years. I have taken a careful look at that chart. I have taken a very careful look at PG&E's resources. It is my opinion that what I hear today in fact reenforces that opinion, that SMUD is about to restart this nuclear powerplant. That the restart of the nuclear plant which provides the least cost option for electricity on the long term SMUD ratepayers. PG&E has come out of the box at this point in time specifically because that restart now appears so close. This is PG&E's only chance to take over SMUD.

For the past fifteen years if my company not had the choice between PG&E and SMUD or Santa Clara, it would have cost us probably in the range of \$4 million a year extra for electricity purchases. If you see on that chart today the rates and basic costs for the two utilities are not that far apart.

They are as close as they have ever been. That's because of two major reasons. You heard essentially a lot about one reason. I want to tell you a little bit about the second one.

From SMUD's standpoint the outages of the Rancho Seco Nuclear Plant since December 1985 has caused two costs. One the extra amount of money they had to spend to restart the plant in terms of capital improvement. The second one is the extra cost of purchasing replacement power. The extra cost of purchasing replacement power goes directly from the pockets of the citizens and the ratepayers in Sacramento into the pocket of PG&E. Because hundreds and thousands of dollars every day Rancho Seco doesn't run, that money is paid to PG&E which provides replacement power. That has driven up the costs that everyone is well aware of electricity in SMUD. From the PG&E's standpoint, the standpoint of their rates, a substantial portion of PG&E's electricity is generated from natural gas. That is very different from the situation at SMUD which relies on hydroelectric power and nuclear power. As we know in 1973 we had a major oil shock, and natural gas prices increased dramatically. As a result, PG&E during the 70's had some of the highest industrial rates in the country and SMUD had some of the lowest. Today, natural gas has dropped dramatically. In fact just in the last three years, the price of natural gas in California has gone from approximately \$6 a million BTUs to less than \$2. I don't expect that situation to continue. I don't expect to sit here

five years from now and still be able to buy gas in California for \$1.80 per million BTUs. As a result, I expect the PG&E rates will start to go back up as natural gas goes back up. I expect that to happen to the rest of the country as well. The major advantage to SMUD from my company's standpoint is that it provides an alternative which is not tied to natural gas, which is in turn tied to world's oil situation. SMUD does not depend on fossil fuel.

I didn't describe what my company does with the electricity.

CHAIRWOMAN MOORE: Why don't you teke one minute to do that, because we need to move on.

MR. Butz: Briefly, it represents about 70% of our cost of production. using only electricity, we take the air and liquify it and convert it into oxygen for hospitals and nitrogen for the California Semiconductor Industry. So not only do we spend a lot of dollars per year, but it is an expense that is critical to us and what we need is stable electric costs over the long term. So, I think this merger between PG&E and SMUD would be anticompetitive. Had it occurred several years ago, my company would be economically disadvantaged to a tremendous degree. I don't believe a merger is necessary to solve the Rancho Seco problem. I don't anybody would dispute in this room that we wouldn't be here having this hearing today if Rancho Seco was still running. If it had run like it always have ran, there

wouldn't be this hearing, because SMUD rates would be dramatically lower than they are today. The issue is not that we need a private company to take over public company, and it is not that we need a large company to buy a small company, that is not necessary to solve the Rancho Seco problem. The problem is that Rancho Seco doesn't run. The issue is how do you get it to run.

Now, I have heard the NRC make some more positive statements that I would have expected them to make, and I heard SMUD make more positive statements that I expected them to make. But even beyond that, the issue of the Ranch running again. If it is not possible for SMUD to run the Ranch, what about Duke? Duke has three identical nuclear plants. They run like a clock. They have the best onstream record in the nuclear power. So, it is not the physical facility out there at Rancho Seco that's the problem, it is the way it has been run. SMUD will admit that, and obviously, they are trying to correct it.

In addition, we have heard from Bonneville. We have heard from cogeneration people. There are a lot of alternatives out there to replace the power even if it turns out that restarting the Ranch is not the most cost effective option. One of those options entails the purchase by PG&E. I think a merger only should be considered as an absolute last resort. If there is no other way, and no other alternatives left, one then should we take the drastic step of eliminating vital competition for electricity in Northern California. I put two caveats on that.

I heard a lot about a rate freeze. To me, talk about a rate freeze there is so much fluff. It's meaningless. To me what's important is the actual cost that the utility incurs. Those actual costs are going to be the costs that are going to be passed on to the ratepayers. The freeze is only a temporary rate. It just advantages one group of people and disadvantages the other. Secondly, the economic analysis of Rancho Seco restart has to be done prior to final action. PG&E unequivocally states if they took over this utility they would shut down the plant. How can you shut down a plant which is several months away from restart?. We heard about PG&E incremental costs being 2½¢. The incremental costs for power out of Rancho Seco, just the incremental costs, for nuclear fuel is a penny. So, where does the 4½¢ coming from? Well, the 4½¢ figure, or the 4.2 figure, various figures you have heard thrown around that are much larger than that, are all the costs of Rancho Seco, the labor, the operating, the maintenance, the fuel and the capital as well amortized. A comparable cost to Diablo Canyon is 12¢. That at full cost. That would compare with maybe a 4¢ figure for the Rancho Seco plant. One is what you have here is a resource that can't be duplicated anywhere for less than a third of the price. Even with the amount that SMUD has put into it. I'm told SMUD has a billion -- maybe we will have a billion dollars into this plant. It produces almost 900 megawatt power. That is only one thousand per kilowatt. You can't build a coal

plant for that. You especially couldn't build a coal plant for that in California with the emissions requirements. It would cost you \$1500 to \$2000 per kilowatt, twice the cost of a Rancho Seco in order to duplicate that facility.

The analogy of a car is not a bad one. It is like having a car that you purchased years ago when cars were cheaper. To the extent that you maintained that car and kept that car in tune, that car could continue to run. Now, this car called Rancho Seco wasn't maintained as well as it should have been, I think everybody agrees with that and that's why we have the problems we have today. However, it is being gone over with a fine tooth comb. I believe and the NRC appears to believe, and I'm willing to spend another three months to find that that that car is now going to get a clean bill of health and it is going to run for the next 20 to 30 years.

CHAIRWOMAN MOORE: Thank you for your comments. Mr. Lewis.

MR. ED LEWIS: My name is Ed Lewis, Council of Sacramento Senior Organizations. I have three points that I would like to make. First, the rate hearings for the past 2½ years have been something that should be divisive and frustrating from the point of view of the public. We believe that Section 14403, Section 14403.3 and Section 14403.5 need to be amended to take care some of the things I have put in my written testimony. The general manager's report, for example, is one thing. It is

so complex the public can't read it. The format is terrible. We need to have the opportunity for rules and regulations to be adopted to provide fair and equal treatment when witnesses come before the board. So, we don't have one rule for one person and one rule for another.

CHAIRWOMAN MOORE: They have not established a procedure for handling complaints.

MR. LEWIS: Right. We need to lengthen the hearing process so there are more meetings. So, we don't have the board taking action on the same night as it has the hearing. It is immediate. We don't know whether they have considered all of the ramifications. It is quite complex. We need to study these things and get staff reaction. Therefore, lengthen the hearings and have two or three hearings. I know that sometimes there is an emergency situation, but this can be provided for.

We would also recommend that the board undergo training. The lack of trust of teamwork on the present board is unbelievable. Not only is it unethical procedure, but it is also sometimes, we are told, breaking the law. We think training might help this.

The second point I have a chart there which shows that the residential class, and only the residential class, of SMUD at the present time is paying more than PG&E rates. But worst than that it goes much further down to the 750 kilowatts are less where you find the poor people, the low income, the low user is

penalized most under the present SMUD rates. Something has to be done. It is preposterous and ridiculous when PG&E comes in and say we are going to freeze the rates. I called top officials of PG&E and I explained to them what would happen. They have not retracted or modified their statement one bit. We are reaching out desperately. I have gone out to lines, which are bread lines, and put on old clothes and talked to some of the people out there. They are taking food off the table in order to pay their utility bills. We are deeply concerned for these people.

The third point I would make is this, that is the utility rates in Sacramento county right now, and this committee I hope you will listen very carefully to what I am saying, the utility rates have gone up with SMUD 84% in the last 2½ years. Another utility, our regional sewer when up 48% this year. Sacramento City has the highest utility rate in the entire State. We think this is terrible. It is not only an inequitable tax, we certainly that tax in particular is onerous, because is it humbly paid for by the poor people in the cities where they have to congregate to live.

CHAIRWOMAN MOORE: You know how I feel about that. I share your concern.

MR. LEWIS: On that particular item, ACA 4 becomes a critical item for you to address. I might say this that I am also a member of AARP. They have authorized me today to say they will give a priority item to ACA 4; for the adoption of that

legislation. So you have not only Sacramento county, you have the entire state that would be behind as far as the seniors are concerned. We are hurting. When you take a look at all of the taxes, could you please take a look by county and see what is happening to the people. Suddenly in Sacramento county has become so bad we recognize that somebody needs to look at the garbage rates, water rates, everything that is a utility. Gather that information and see how much the taxes are going up and why people are screaming. Proposition 13 and the Gann Amendments are in force and they are pushing things out through the utilities. I hope that this committee will take a look at that carefully and do something about it.

CHAIRWOMAN MOORE: Thank you very much for your comments.

ASSEMBLYWOMAN WRIGHT: I have legislation that I carried which is presently before Revenue and Taxation Committee which I tried to limit what they called user fees. I have the whole League of California Cities and the boards of supervisors all opposed to that bill. I couldn't even get votes out of that committee. That is one of my concerns that it has been pushed the other way. But, I wanted to asked basically, does SMUD have a minimum rate?

CHAIRWOMAN MOORE: Do you mean a base line, life line?

ASSEMBLYWOMAN WRIGHT: No. I just mean a minimum rate. In other words, if I were just connected to SMUD and I haven't

been there in months in my home and I didn't use it, is there a minimum rate I would have to pay?

MR. LEWIS: Not to my knowledge.

ASSEMBLYWOMAN WRIGHT: I'm on SMUD. I can't figure out my bill.

MR. LATHAM: The District has a service charge, and you would be charged that monthly service charge.

ASSEMBLYWOMAN WRIGHT: What is it?

MR. LATHAM: I think it is about \$2.40 per month.

CHAIRWOMAN MOORE: You would have to request it.

MR. LATHAM: It's automatic. What it covers is meter reading costs, the billing costs and those sort of things.

ASSEMBLYWOMAN WRIGHT: I haven't been to my place for a month and I got a bill for \$25. I'm trying to figure that one out.

CHAIRWOMAN MOORE: That's what I'm saying, it is not an automatic if it is just a monthly service. What she is trying to say is there a minimum rate when the house is unoccupied or something, is there a rate?

MR. LATHAM: It's the customer charge that I am describing. If there weren't any energy used at all, it would be a customer of about \$2.40 per month. It simply covers the costs of having the meter there.

CHAIRWOMAN MOORE: I guess we all live in Sacramento and we are all not here for long period of time. We have never seen any \$2.40 bill.

MR. LATHAM: The refrigerator runs, those sort of things.

CHAIRWOMAN MOORE: Let me thank the people who participated on the various panels. I think it has been very informative. I think the reason why we came here is to better understand the proposal by PG&E to SMUD, to get some reaction and to also take a look at the other resources that were out there. I think the presentations that were made, made it very clear to us that this is indeed an issue that we will be looking at for a long time to come. There have been some recommendations for legislation. We will take a look at those. We will be analyzing those and you will be hearing from us in the not too distant future.

Again, let me say thank you to each and every one.

ASSEMBLYWOMAN WRIGHT: I would like to tell the elected board of SMUD to take heed to serve you here and start listening to the people out there.

CHAIRWOMAN MOORE: With those comments, I would like to adjourn this hearing. Thank you very much for coming.

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California Legislature

Assembly Committee

on

Utilities and Commerce

GWEN MOORE

CHAIRWOMAN
MEMBER OF THE ASSEMBLY
FORTY-NINTH DISTRICT

September 18, 1987

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Hon. Cliff Wilcox
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Hon. Richard A. Clarke
Chairman of the Board
Pacific Gas & Electric Company
77 Beale Street
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Dear Sirs:

The Assembly Utilities & Commerce Committee will conduct a hearing on the proposal of Pacific Gas & Electric Company to consolidate the electric operations of the Sacramento Municipal Utility District (SMUD) with the rest of its Northern California operations. The hearing is scheduled for October 6, 1987 at the Capitol in Sacramento.

The hearing will focus on the PG & E proposal, the views of SMUD and other interested parties on the proposal, and other options for SMUD and its customer-owners, including the State of California.

PG & E's offer to buy SMUD is potentially a watershed in the history of energy supply in Northern California. Northern California demonstrates great variety in the types of public and private entities that provide water and power to our citizens. SMUD is the largest publicly-owned utility in Northern California and is the key to maintaining that diversity. I believe that that diversity and the healthy competition it sustains are extremely valuable. Under normal circumstances I would consider a proposal to take over SMUD flatly unacceptable, because of the potential for fundamentally altering the relationship between public and private power companies in California.

Present circumstances are not normal, however. There are a number of pragmatic reasons why the unacceptable appears quite attractive. At the top of the list is the uncertainty surrounding Rancho Seco. It is apparent that the lengthy Rancho Seco outage has negated some of the economic advantages that SMUD enjoys as a utility -- the low interest rates; populous, dense and growing service area; the access to low-cost hydroelectricity and federally subsidized power. SMUD rates have been climbing steadily at a time when rates for all other electric utilities in California have been stable or declining, and all other energy prices have been falling. The prolonged stress caused by these developments has sapped SMUD's institutional strength and credibility, as well as its finances.

This trend can be reversed, if Rancho Seco is restarted and operates reliably for a period of several years. However, restart is extremely uncertain, putting to one side the pending ballot measure on permanent closure, and the generic concerns with nuclear reactors of the type installed at Rancho Seco. SMUD's basic ability to comply with the terms of its operating license has been called into question. With the ongoing instability at higher management levels, it is not clear what SMUD must do to satisfy the Nuclear Regulatory Commission under any circumstances. We need clarification on this point, as well as a clear assessment of the non-nuclear supply options for the District.

PG & E has the size and financial ability to withstand a substantial write-off that closure of Rancho Seco would represent. The offer to accept responsibility for closure and decommissioning focuses the fact that SMUD has substantial contingent liabilities that will affect rates in the not-too-distant future. The same point applies to PG & E's offer to settle the litigation before the Federal Energy Regulatory Commission, in which PG & E seeks damages from SMUD for alleged failure to perform SMUD's end of the bargain to furnish energy and capacity from Rancho Seco. Any appreciable assessment of damages in that suit could raise rates an additional amount for an uncertain period of time.

PG & E also has substantial uncertainties that will affect rates. Conclusion of the Diablo Canyon rate case in PG & E's favor will raise rates in Northern California as much as 15 %, wiping out any savings SMUD customers might realize from consolidation. Conclusion of that case in the ratepayers' favor, (in accordance with the PUC Staff recommendation of a \$4 billion write-down, for example), may diminish the financial strength that PG & E counts on to sustain it through a major write-off.

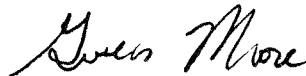
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PG & E's proposal of a rate freeze at a time when SMUD rates are at a historic high is, truly, cold comfort to ratepayers who are told to expect rates to go down once Rancho Seco is resolved, one way or another. The business community in particular could be disadvantaged relative to other PG & E customers if rate design proposals currently under consideration at the PUC are adopted, affording PG & E the right to selectively discount rates for favored business customers, but denied to Sacramento area customers.

At the hearing, I would like a frank exploration of these issues, and others raised by the proposal, including whether enabling legislation is required to effectuate the consolidation or any other options available to SMUD, and the potential "ripple effects" on other public power agencies.

I look forward to your cooperation and assistance in publicly exploring this dramatic and challenging development. Please contact Bill Julian and Tyrone Netters of my staff to coordinate your presentations.

Yours sincerely,



GWEN MOORE,
Chairwoman

GM:wj

**COMMENTS OF JOHN KEHOE
MEMBER
BOARD OF DIRECTORS**

SACRAMENTO MUNICIPAL UTILITY DISTRICT

**For the
ASSEMBLY COMMITTEE ON UTILITIES AND COMMERCE**

Honorable Gwen Moore, Chairwoman

**Interim Hearing on
Proposed Consolidation of SMUD and PG&E
October 6, 1987**

Good morning Chairwoman Moore and members of the committee. My name is John Kehoe. I am a member of the Board of Directors of the Sacramento Municipal Utility District.

First, let me thank the Committee for holding this hearing and for giving us the opportunity to appear before you today. We at SMUD understand and support your Committee's interest in our utility and in the economic and policy issues raised by PG&E's "consolidation" idea. This idea, first put forth in Chairman Clarke's September 3 letter raises the prospect of radical change, not only for Sacramento, but for the utility industry statewide, even nationally. Your Committee's prompt action in calling this hearing, barely a month since Mr. Clarke's letter, suggests that you share this perception.

My remarks this morning will be very brief. I intend only to provide a little background by describing the District and what the Board of Directors sees as its role in this matter. I will then introduce Mr. William K. Latham, SMUD's acting General Manager, who will provide the District's current perspective on the "consolidation" idea.

What is SMUD? SMUD is a local public agency organized under the Municipal Utility District Act (Div. 6 of the Public Utilities Code) with which your Committee is no doubt familiar. As a municipal utility district, the District is governed by a five-member board of directors, elected by ward for staggered four-year terms. Two of my fellow Board members are present here this morning.

SMUD was originally formed by a vote of the people in 1923, but did not begin providing electric service until 1947, nearly a quarter century later. This long delay was attributable in large part to the determined opposition of the Pacific Gas & Electric Company which was then providing electricity in Sacramento. For the past 40 years, SMUD has been the sole distributor of electricity within its service area which now comprises most of Sacramento County and a small portion of Placer County. This service area is about 900 square miles and contains over 900,000 people (400,000 electric customers) making SMUD one of the largest consumer-owned electric systems in the country.

Until quite recently, our 40 year operating history has been an unqualified success. We have grown from 71,000 customers with a peak demand of 77 MW in 1947 to over 400,000 customers with a peak demand of 1902 MW in 1987. In 1947, we purchased all of our electricity from PG&E. During the past 40 years we have developed and built 1695 MW of our own generating capacity, including hydroelectric, nuclear, geothermal, photovoltaic and combustion turbine units. We have also secured a long-term firm power supply of 360 MW from the Western Area Power Administration and have acquired transmission rights on the Pacific Northwest Intertie over which we purchase power from Northwest Utilities. Over the past decade we have developed substantial, innovative demand side management programs as well. These efforts have, until very recently, allowed SMUD to meet the needs of one of California's most rapidly growing areas with safe, reliable, low-cost electricity. This is a record of which the District and the Sacramento community can be proud.

Unfortunately, the last 3 or 4 years have seen an abrupt departure from this remarkably successful trend. Operating and management problems at Rancho Seco (SMUD's 913 MW nuclear power plant), including the current outage which has lasted 21 months and is expected to last another three or four, have contributed significantly to a rapid escalation of rates and to a weakening of the District's financial condition. Since 1984, our rates have increased from 53% to 89% of PG&E's electric rates on a system average basis. These increases, together with the notoriety surrounding events at Rancho Seco, have increased public concern about the District to a very high level and no doubt contributed to PG&E's decision to propose "consolidation" with the District.

As the elected representatives of SMUD's consumer-owners, the Board of Directors must take ultimate responsibility for the District's recent problems. We are also expected to take responsibility for solving these problems in a way which can assure the future reliable supply of reasonably priced electricity which our consumer-owners rightly expect. We do not shrink from that responsibility. I am here today to assure your committee and this community that we are determined to discharge our responsibilities so as to assure the best long-term interests of our consumer-owners.

In fact, we have not been idle in the face of these problems. By 1983, The Board was becoming increasingly concerned with potential problems at Rancho Seco. A 1984 study commissioned by the Board identified a number of corrective actions that needed taking and we began to implement those actions in early 1985. Unfortunately, progress was not rapid enough to

avoid a series of outages that year, culminating in the December 26 incident which resulted in the current extended shut-down.

Much more drastic and far-reaching changes at Rancho Seco have been made since then, and they have cost enormous sums of money. Recognizing that Rancho Seco was too large a financial risk and operating responsibility for a utility of SMUD's size, absent the integration agreement with PG&E, we also commenced an aggressive program to reduce that risk and responsibility. More recently, the District undertook an unprecedented solicitation of power supply proposals from all sources, including utilities and independent producers.

Notwithstanding the substantial publicity surrounding PG&E's September 3 letter, we view the "consolidation" idea as one of several creative ideas to emerge from the District risk reduction program, which is what we call our effort to reduce our financial and operational risks associated with Rancho Seco. We view "consolidation" and the other divestiture ideas as one set of options for the District. Our power supply solicitation efforts (RFP) have resulted in approximately 50 proposals totaling over 6,000 MW of potential power, which, taken singly or in various combinations, provide additional options. And finally, our determined efforts to improve safety, reliability and efficiency at Rancho seco are resulting in substantial and encouraging progress.

All of these opportunities have led me to be more optimistic, more hopeful about SMUD's future than at any time since I have been on the Board of Directors.

With that background, I would like to introduce Bill Latham, our acting General Manager. Bill will describe SMUD's current situation and our assessment of our options including the idea of consolidating with PG&E. He is a veteran of 26 years service with the District, and is an electrical engineer with a great deal of experience in utility operations. He has served as acting General Manager for the past 14 months.

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COMMENTS OF BILL LATHAM
ACTING GENERAL MANAGER
SACRAMENTO MUNICIPAL UTILITY DISTRICT

FOR THE
ASSEMBLY COMMITTEE ON UTILITIES AND COMMERCE
HONORABLE GWEN MOORE, CHAIRWOMAN

INTERIM HEARING ON
PROPOSED CONSOLIDATION OF SMUD AND PG&E
OCTOBER 6, 1987

THANK YOU MR. KEHOE. GOOD MORNING MADAM CHAIRWOMAN, MEMBERS, LADIES AND GENTLEMEN. I SHARE MR. KEHOE'S ENTHUSIASM FOR THE FUTURE OF SMUD. PERHAPS SMUD'S VIEW OF THE "CONSOLIDATION IDEA" CAN BEST BE UNDERSTOOD IN THE CONTEXT OF OUR CURRENT SITUATION.

SMUD'S CURRENT SITUATION

RESOURCE BASE: AT PRESENT, THE DISTRICT'S MAJOR GENERATING FACILITIES CONSIST OF SEVEN HYDROELECTRIC PLANTS, COLLECTIVELY KNOWN AS THE UPPER AMERICAN RIVER PROJECT, WITH A TOTAL INSTALLED CAPACITY OF APPROXIMATELY 659 MEGAWATTS; THE RANCHO SECO NUCLEAR PLANT, WITH AN INSTALLED NET CAPACITY OF 913 MEGAWATTS, A 72 MEGAWATT GEOTHERMAL STEAM ELECTRIC GENERATING PLANT, AND A 49 MEGAWATT COMBUSTION TURBINE. IN ADDITION, SMUD HAS 65 MW OF GEOTHERMAL UNDER CONSTRUCTION IN JOINT VENTURE AGREEMENTS WITH THE PUBLIC AGENCIES IN NORTHERN CALIFORNIA. SMUD ALSO HAS A LONG-TERM POWER PURCHASE AGREEMENT WITH THE WESTERN AREA POWER ADMINISTRATION FOR 360 MEGAWATTS OF FIRM POWER AND A TRANSMISSION AGREEMENT FOR 200 MW OF POWER BETWEEN THE PACIFIC NORTHWEST AND SMUD. SMUD ALSO HAS A POWER SALE EXCHANGE AND INTEGRATION AGREEMENT WITH PG&E.

PG&E AGREEMENT: THE AGREEMENT WITH PG&E HAS BEEN AN INTEGRAL PART OF SMUD'S RESOURCE MIX. IN GENERAL TERMS, THE CONTRACT WAS STRUCTURED SUCH THAT SMUD WOULD BENEFIT FROM RESERVE

SHARING AND THE ECONOMIES OF SCALE ASSOCIATED WITH A LARGE NUCLEAR PLANT, AND PGANDE WOULD BENEFIT FROM PURCHASING SMUD SURPLUS FIRM CAPACITY AND ENERGY AT SMUD'S PRODUCTION COST WHICH WAS LOWER THAN PGANDE'S ALTERNATIVES.

THE PRINCIPAL FEATURE OF THE CONTRACT IS THAT PARTIES SHARE RESERVES SO THAT IN THE EVENT OF AN OUTAGE OF EITHER GENERATION OR TRANSMISSION, THE RESOURCES OF THE ENTIRE INTERCONNECTED SYSTEM ARE AVAILABLE TO MEET LOADS. PGANDE PURCHASES NEARLY ALL CAPACITY AND ENERGY PRODUCED BY THE DISTRICT WHICH IS SURPLUS TO THE DISTRICT'S REQUIREMENTS. THIS ALLOWS THE DISTRICT TO OPERATE ITS RESOURCES AT A HIGH CAPACITY FACTOR SO THAT THE COST PER KILOWATT HOUR OF ENERGY CAN BE HELD TO A MINIMUM. IF THE DISTRICT'S GENERATION IS LESS THAN ITS REQUIREMENTS, PGANDE MAKES CAPACITY AND ENERGY AVAILABLE TO SMUD ON AN EXCHANGE BASIS. THE ENERGY PROVIDED IS SUBJECT TO ANNUAL ENERGY BORROWING LIMITS. THE AGREEMENT HAS BEEN AMENDED TWICE AND WILL EXPIRE DECEMBER 31, 1989. THE CONTRACT STATES THAT THE PARTIES WILL ATTEMPT TO NEGOTIATE A LONG-TERM INTERCONNECTION AGREEMENT FOR THE FUTURE AND THAT IF SUCH A CONTRACT CANNOT BE NEGOTIATED, PGANDE IS REQUIRED TO FILE WITH THE FEDERAL ENERGY REGULATORY COMMISSION A NEW RATE SCHEDULE UNDER WHICH PGANDE WILL PROVIDE THE DISTRICT THE SERVICES IT NEEDS AFTER DECEMBER 31, 1989.

LITIGATION OF AGREEMENT: ALTHOUGH ALL OF SMUD'S MAJOR GENERATION RESOURCES ARE COVERED IN THE AGREEMENT, THE CURRENT

OUTAGE OF THE RANCHO SECO NUCLEAR POWER PLANT HAS CAUSED PG&E TO FOCUS PRIMARILY ON THAT PLANT AND TO SEEK A UNILATERAL CHANGE OF THE TERMS OF THE INTEGRATION AGREEMENT. THIS, OF COURSE, HAS RESULTED IN LITIGATION.

IN FEBRUARY 1986, PG&E NOTIFIED THE DISTRICT THAT IT WOULD NO LONGER MAKE PAYMENTS TO SMUD AS REQUIRED UNDER THE CONTRACT FOR RANCHO SECO CAPACITY UNTIL RANCHO SECO WAS RESTARTED AND OPERATED RELIABLY.

PG&E HAS ALSO TOLD THE DISTRICT THAT PG&E BELIEVES THAT THE RATED CAPABILITY OF RANCHO SECO HAS CHANGED FROM 913 MW TO 0. THE DISTRICT BELIEVES THAT THE CURRENT RANCHO SECO OUTAGE CONSTITUTES A "SHORT-TIME CURTAILMENT" WITHIN THE MEANING OF THE CONTRACT. SHORT-TIME CURTAILMENTS ARE NOT A BASIS FOR A RERATING OF RANCHO SECO UNDER THE CONTRACT, IF THE DISTRICT USES "DUE DILIGENCE" TO RETURN THE PLANT TO SERVICE. THE DISTRICT IS MEETING THIS OBLIGATION. IN 1986 THE DISTRICT FILED A COMPLAINT WITH FERC ASKING FOR A RULING TO THAT EFFECT.

THE DISPUTE IS EXCEEDINGLY COMPLEX. ALTHOUGH PG&E MAY DISAGREE WITH THE NUMBERS, SMUD BELIEVES THAT REALISTICALLY APPROXIMATELY \$22 MILLION IN CAPACITY PAYMENTS IS AT STAKE. ADDITIONALLY, IF SMUD LOSES, SMUD MUST DELIVER TO PG&E SUBSTANTIAL QUANTITIES OF SURPLUS CAPACITY, WHICH SMUD WILL HAVE AVAILABLE IF OFF PEAK MONTHS. THE FERC PROCEEDING IS NOW IN TRIAL IN WASHINGTON, DC.

FINANCIAL/OPERATING CONDITIONS

FOLLOWING MANY YEARS OF A VERY STRONG FINANCIAL CONDITION AND A AA BOND RATING, THE DISTRICT HAS MOST RECENTLY REPORTED NET LOSSES OF \$9.2 MILLION IN 1985 AND \$3.7 MILLION IN 1986, AND A CORRESPONDING GRADUAL LOWERING OF THE DISTRICT'S BOND RATING TO A BBB RATING. THE EXTENDED OUTAGE AT RANCHO SECO HAS HAD A MAJOR IMPACT ON THE DISTRICT'S FINANCIAL AND OPERATING CONDITIONS RESULTING IN INCREASED O&M EXPENSES TO RESTART THE PLANT, ADDITIONAL PURCHASED POWER REQUIREMENTS AND A DECREASE IN INCOME FROM THE SALE OF SURPLUS RANCHO SECO POWER.

WITH THE RESTART OF RANCHO SECO AT HAND AND THE RESULTS OF RECENT ACTIONS OF THE DISTRICT TO RESTORE ITS FINANCIAL HEALTH--OUR FINANCIAL PICTURE IS STABILIZED. NET INCOME FOR THE FIRST HALF OF 1987 WAS \$8.7 MILLION, WITH ANNUAL 1987 NET INCOME PROJECTED TO BE \$12 MILLION. THE DISTRICT'S LIQUIDITY THROUGH MID-1988 IS ASSURED BY A \$150 MILLION BOND SALE EXECUTED JUST LAST WEEK.

THE 1987 BUDGET IS \$832 MILLION, WHICH INCLUDES \$240 MILLION FOR RESTART OF RANCHO SECO AND APPROXIMATELY \$200 MILLION FOR POWER PURCHASES. THE ORIGINAL 1988 BUDGET REQUEST IS FOR \$759 MILLION, OR ABOUT NINE PERCENT BELOW THE 1988 BUDGET AMOUNT.

THIS PROVIDES YOU WITH A BRIEF OVERVIEW OF THE DISTRICT'S CURRENT SITUATION. I'D LIKE TO MOVE NOW TO OUR OPTIONS FOR THE FUTURE.

OPTIONS FOR THE FUTURE

"RISK REDUCTION" OPTIONS: LAST YEAR, IN VIEW OF THE 1989 TERMINATION OF THE PGANDE INTEGRATION CONTRACT, THE DISTRICT EMBARKED ON A FINANCIAL AND OPERATIONAL RISK REDUCTION PROGRAM WITH RESPECT TO ITS GENERATING FACILITIES, SPECIFICALLY RANCHO SECO.

AS A RESULT OF THIS EFFORT, THE DISTRICT HAS IDENTIFIED SEVERAL OPTIONS AVAILABLE TO US, INCLUDING:

1. OPERATING RANCHO SECO AND SELLING A PORTION OF ITS OUTPUT.
2. TRANSFERRING THE OWNERSHIP AND OPERATION OF RANCHO SECO TO ANOTHER ENTITY.
3. RECONFIGURING THE ELECTRIC SYSTEM.
4. REPOWERING RANCHO SECO.

(1) OPERATE RANCHO SECO AND SELL POWER

UNDER THIS SCENARIO, SMUD WOULD RESTART AND OPERATE RANCHO SECO UNDER THE CURRENT AGREEMENT WITH PGANDE UNTIL 1990 AND THEN ENTER INTO CONTRACTS WITH OTHER UTILITIES TO SELL OR EXCHANGE A PORTION OF RANCHO SECO POWER. THE NEED FOR RESOURCES TO REPLACE ANY TRANSFERRED PORTION OF RANCHO

SECO AND TO MEET LOAD GROWTH WOULD BE MET BY INTERCONNECTION ARRANGEMENTS WITH PG&E, INTERCONNECTION ARRANGEMENTS WITH OTHER UTILITIES AS PLANNED TRANSMISSION INTERTIE PROJECTS ARE COMPLETED, CONSTRUCTION OF RESOURCES TO THE EXTENT POSSIBLE, AND PURCHASES OF RESOURCES FROM INDEPENDENT POWER PRODUCERS AND OTHER UTILITIES. SINCE SMUD DOES NOT HAVE THE NEED FOR ALL OF THE BASELOAD CAPABILITY OF RANCHO SECO, REPLACEMENT POWER WOULD CONSIST OF PEAKING AND INTERMEDIATE TYPE RESOURCES IN THE NEAR TERM WHICH ARE GENERALLY LESS EXPENSIVE THAN BASELOAD POWER.

(2) TRANSFER OF OWNERSHIP AND OPERATION OF RANCHO SECO

THE DISTRICT HAS DISCUSSED THE PROPOSED TRANSFER OF OPERATING RESPONSIBILITIES AND OWNERSHIP AT RANCHO SECO WITH POTENTIAL TRANSFEREES. THE DISTRICT RECOGNIZES THAT A POTENTIAL TRANSFEREE, IN ORDER TO FULLY ASSESS OWNERSHIP OF RANCHO SECO, MAY AGREE TO ACQUIRE ONLY AN OPTION TO PURCHASE RANCHO SECO AND OPERATE RANCHO SECO DURING THE PERIOD OF SUCH OPTION. THE DISTRICT BELIEVES THAT SUCH AN OPTION PERIOD WOULD EXTEND FOR AT LEAST TWO TO FIVE YEARS.

ANY TRANSFER OF OWNERSHIP OF RANCHO SECO WOULD BE MADE IN CONSIDERATION OF AN AGREEMENT FOR POWER SUPPLY SERVICES FROM THE TRANSFEREE.

(3) SYSTEM RESTRUCTURE AND RECONFIGURATION

IN CONNECTION WITH THE POSSIBLE RECONFIGURATION OF THE ELECTRIC SYSTEM, THE DISTRICT IS ENGAGED IN PRELIMINARY DISCUSSIONS WITH SEVERAL UTILITIES THAT HAVE EXPRESSED AN INTEREST IN ESTABLISHING ANOTHER ENTITY FOR THE PURPOSE OF HOLDING ALL OR A PORTION OF THE DISTRICT'S GENERATION AND TRANSMISSION RESOURCES, INCLUDING RANCHO SECO. THIS ENTITY WOULD THEN SELL THE DISTRICT A PORTION OF THE POWER FROM THESE RESOURCES UNDER A FAVORABLE CONTRACT.

Portland Gas & Electric / Diesel Power / possibly RPA —
(4) REPOWER RANCHO SECO *put together by investment bankers;*

THE DISTRICT BELIEVES THAT CONVERSION OF RANCHO SECO TO A NATURAL GAS-FIRED RESOURCE MAY BE TECHNICALLY AND ECONOMICALLY FEASIBLE. HOWEVER, SIGNIFICANT REGULATORY OBSTACLES MUST BE OVERCOME IN ORDER TO COMPLETE CONVERSION TO SUCH A FUEL SOURCE. THESE INCLUDE, AMONG OTHERS, COMPLIANCE WITH FEDERAL, STATE AND LOCAL EMISSIONS STANDARDS AND COMPLIANCE WITH NRC REGULATIONS REGARDING SPENT FUEL STORAGE. THE DISTRICT IS STUDYING THIS ALTERNATIVE AND IS DISCUSSING IT WITH A BULK GAS SUPPLIER.

THE REPOWERING OPTION COULD BE COMBINED WITH OPTIONS BASED ON ESTABLISHING A GENERATING COMPANY FOR TRANSFER OF OWNERSHIP OF RANCHO SECO.

ASSUMING THAT DESIGN AND PREPARATION FOR THE REPOWERING COULD TAKE AS LONG AS TWO YEARS, SMUD COULD CONTINUE TO

OPERATE RANCHO SECO AND RELY ON THE EXISTING PG&E CONTRACT UNTIL 1990. BEGINNING IN 1990, SMUD WOULD TERMINATE NUCLEAR OPERATIONS OF RANCHO SECO, BUY SHORT TERM POWER FROM OTHER SUPPLIERS AND COMMENCE OPERATION OF THE REPOWERED FACILITIES IN 1992.

PURCHASE POWER RFP: IN ORDER TO EXPAND THE DIVESTITURE OPTIONS AND DETERMINE THE COST AND AVAILABILITY OF POWER WHICH CAN BE USED TO MEET THE DISTRICT'S NEED FOR POWER WITH OR WITHOUT RANCHO SECO, THE DISTRICT ISSUED A REQUEST IN AUGUST OF THIS YEAR. IN RESPONSE TO THE REQUEST FOR PROPOSALS, THE DISTRICT RECEIVED 49 PROPOSALS DESCRIBING OVER 6,000 MW OF POWER RESOURCES. IN ADDITION, THE DISTRICT IS EVALUATING GENERATION AND TRANSMISSION PROJECTS AND DEMAND-SIDE PROGRAMS WHICH WILL PROVIDE EVEN MORE OPTIONS FOR MEETING ITS LOAD. THESE INCLUDE LOCAL COGENERATION PROJECTS, A COMPRESSED AIR ENERGY STORAGE PROJECT, ADDITIONS TO THE DISTRICT'S EXISTING HYDROELECTRIC PROJECTS, AND A TRANSMISSION LINE TO CONNECT THE DISTRICT WITH COAL GENERATION IN NEVADA AND THE NORTHWEST.

ALTHOUGH MANY OF THE RESPONSES TO THE REQUEST FOR PROPOSALS DESCRIBED POWER WHICH WOULD BE AVAILABLE ONLY AFTER COMPLETION OF CONSTRUCTION OF EITHER GENERATING STATIONS OR TRANSMISSION LINES, SEVERAL OF THE RESPONSES FROM UTILITIES DESCRIBED SURPLUSES OF POWER WHICH COULD BE MADE AVAILABLE TO THE DISTRICT IMMEDIATELY. THESE INCLUDE OFFERS FROM PG&E, THE BONNEVILLE POWER ADMINISTRATION, AND SOUTHERN CALIFORNIA

EDISON. THE DISTRICT WILL EVALUATE ALL OF THE OFFERS TO DETERMINE WHETHER THE POWER OFFERED UNDER THOSE PROPOSALS IS AT A PRICE WHICH IS LESS THAN THE CONTINUED COSTS OF OPERATING RANCHO SECO. IN ADDITION, THE OFFERS WILL BE USED TO DETERMINE HOW BEST TO MEET THE DISTRICT'S NEEDS FOR POWER SERVICES TO BACK UP OR SUPPLEMENT RANCHO SECO.

PGANDE CONSOLIDATION

PGANDE HAS ALREADY DESCRIBED ITS PROPOSAL OF CONSOLIDATION TO YOU TODAY. THE PROPOSAL RAISES A NUMBER OF ISSUES, INCLUDING PRICE OFFERED BY PGANDE, RATE FREEZE DURATION AND SUBSEQUENT RATE LEVELS, RANCHO SECO TERMINATION, TAXES AND PROFIT MARGINS AND LOCAL CONTROL.

EVALUATION PROCESS

RATE IMPACTS OF OPTIONS: THE MOST VALID WAY TO EVALUATE THE OPTIONS FOR SMUD IS TO COMPARE EXPECTED RATES FOR THE SACRAMENTO COMMUNITY. IN A RECENT SUBMITTAL TO THE CALIFORNIA ENERGY COMMISSION, PG&E FORECASTS ITS SYSTEM AVERAGE RATES TO ITS CUSTOMERS TO RISE TO ABOUT 10.5¢ PER KILOWATT HOUR BY 1990. EVEN IF PG&E SUCCEEDS IN GETTING ONLY A FRACTION OF DIABLO CANYON COSTS INTO ITS RATE BASE, THEIR SYSTEM AVERAGE RATES WILL RISE TO OVER 9¢ PER KILOWATT HOUR BY THAT YEAR.

THE 1990 RATES TO SACRAMENTO CUSTOMERS FOR SMUD'S RANGE OF OPTIONS ARE BELOW THE LOWEST RATES FORECAST FOR PG&E TO ITS

CUSTOMERS. SMUD IS UNDERTAKING A "RISK REDUCTION" PROGRAM WHICH WILL NARROW DOWN THE POTENTIAL RANGE OF SMUD RATES AND INCREASE THE CONFIDENCE WE HAVE IN FORECASTING RATES FOR 1990 AND BEYOND. THE RATES FOR THE "RISK REDUCTION" OPTIONS RANGE FROM UNDER 8¢ TO ABOUT 8.5¢ PER KILOWATT HOUR FOR 1990.

THE LOW END OF THIS RANGE IS ASSOCIATED WITH OPERATING RANCHO SECO, DIVESTING OWNERSHIP TO AN EXPERT OPERATOR, AND PURCHASING SOME OF THE POWER FROM THE NEW OWNER. ALTERNATIVELY, IF RANCHO SECO WERE SHUT DOWN AND POWER PURCHASED FROM PG&E AND OTHERS, SMUD RATES WOULD BE NEAR THE UPPER END OF THE "RISK REDUCTION" OPTION RANGE. SMUD AVERAGE RATES WOULD STILL BE BELOW PG&E'S AVERAGE RATES.

PG&E'S OFFER TO TAKE OVER SMUD AND "FREEZE RATES," WHILE POLITICALLY PERSUASIVE, WOULD APPARENTLY BE ONLY A TEMPORARY RESPITE FROM THE HIGHER RATES PG&E CUSTOMERS MUST PAY.

WE EXPECT SMUD RATES TO BE WELL UNDER PG&E'S RATES WHETHER RANCHO SECO IS OPERATED OR SHUT DOWN.

DEVELOPMENT AND SELECTION OF OPTIONS: PRELIMINARY ASSESSMENTS INDICATE THAT FROM THE STANDPOINT OF FUTURE RATES, THE ALTERNATIVES APPEAR PREFERABLE TO CONSOLIDATION WITH PG&E. HOWEVER, OTHER FACTORS SUCH AS RATE STABILITY, SUPPLY RELIABILITY, FINANCIAL RISKS, CAPITAL COSTS, AND, OF PARAMOUNT IMPORTANCE, FEASIBILITY, MUST BE TAKEN INTO ACCOUNT.

CONSEQUENTLY, IT IS OUR PLAN TO CONTINUE WITH THE DEVELOPMENT, REFINEMENT AND THOROUGH EVALUATION OF EACH PROMISING OPTION, INCLUDING POSSIBLE CONSOLIDATION, ON AN EQUAL BASIS. AS WE PROCEED, OPTIONS WHICH LOOK LESS PROMISING WHEN MEASURED AGAINST ONE OR MORE OF THE ABOVE CRITERIA, WILL BE SET ASIDE IN FAVOR OF THE MORE PROMISING OPTIONS. THROUGH THIS PROCESS, WE WILL SETTLE ON THE MOST PROMISING OPTION OR COMBINATION OF OPTIONS. BY EARLY NEXT YEAR, WE EXPECT TO HAVE REDUCED THE OPTIONS TO THE ONE, OR PERHAPS TWO, MOST PROMISING ALTERNATIVES AND TO HAVE SUBSTANTIALLY COMPLETED THE DETAILED DISCUSSIONS NEEDED TO REACH AGREEMENT WITH THE PARTIES INVOLVED.

WE HAVE ALREADY ENGAGED ENGINEERING AND SPECIALTY CONSULTANTS TO ASSIST IN THIS DEVELOPMENT AND SELECTION PROCESS, AND WE HOPE TO ENGAGE ADDITIONAL OUTSIDE EXPERTISE, INCLUDING FINANCIAL SPECIALISTS, IN THE VERY NEAR FUTURE.

IT IS IMPORTANT TO POINT OUT AT THIS TIME THAT THE CONTINUED SOLE OWNERSHIP AND OPERATION OF RANCHO SECO IS NOT A DESIRABLE LONG-TERM OPTION. ALTHOUGH THIS OPTION WOULD RESULT IN POTENTIALLY THE LOWEST RATES OF ANY, ITS DRAWBACKS, INCLUDING FINANCIAL AND OPERATING RISKS AND CAPITAL COSTS, MAKE IT RELATIVELY UNATTRACTIVE. FURTHERMORE, THE OPTION OF REPOWERING RANCHO SECO, WHILE VERY INTRIGUING, WOULD REQUIRE, AT BEST, THREE TO FOUR YEARS TO IMPLEMENT, AND THUS IS NOT QUITE COMPARABLE TO THE

REMAINING OPTIONS WHICH AT LEAST POTENTIALLY COULD BE IMPLEMENTED VERY QUICKLY.

FINALLY, ON THE MATTER OF THE AVAILABLE OPTIONS, IT IS ESSENTIAL TO REALIZE THAT EACH OF THEM, TO SOME IMPORTANT DEGREE, INVOLVES ACCESS TO TRANSMISSION WHICH IS CONTROLLED BY PG&E. PRESUMABLY, PG&E FORESEES NO PROBLEM DELIVERING POWER TO THE DISTRICT IF CONSOLIDATION WERE TO TAKE PLACE. VERY PROBABLY, THE CENTRAL ISSUE DURING THE NEXT SEVERAL MONTHS WILL BE WHETHER TRANSMISSION IS AS READILY AVAILABLE UNDER THE OTHER OPTIONS. MR. FRANK HAHN, THE DISTRICT'S WITNESS ON THE PANEL ON RESOURCE OPTIONS AND TRANSMISSION ACCESS, WILL ADDRESS THIS ISSUE IN MORE DETAIL AT THAT TIME.

RATES AND RATE POLICIES

NOW, LET ME CONCLUDE MY REMARKS BY TURNING BRIEFLY TO ANOTHER TOPIC IN WHICH THE COMMITTEE HAS EXPRESSED INTEREST: RATE SETTING POLICIES AND PROCEDURES.

RATE LEVELS AND STRUCTURE: DISTRICT RATE LEVELS HAVE HISTORICALLY BEEN VERY COMPETITIVE WITH THE RATES OF OTHER UTILITIES WITHIN THE STATE AND THROUGHOUT THE NATION. THIS COMPETITIVE EDGE HAS NARROWED SOMEWHAT AS A RESULT OF A SERIES OF 5 RATE ACTIONS FROM 1985 TO THE PRESENT, NEEDED TO MEET SYSTEM GROWTH AND TO SUPPORT THE OUTAGE AT RANCHO SECO.

DESPITE THESE RATE INCREASES, IT IS IMPORTANT TO NOTE THAT THE SMUD SYSTEM RATES ARE STILL LOWER THAN PG&E SYSTEM RATES. THE DISTRICT ESTIMATES ITS SYSTEM AVERAGE RATE AT 6.8¢/KWH, WHICH IS MORE THAN 10% BELOW THE PG&E SYSTEM AVERAGE RATE.

DISTRICT RATES HISTORICALLY ARE COST-BASED. DISTRICT POLICY IS TO FURNISH RELIABLE ELECTRIC SERVICE AT THE LOWEST RATES CONSISTENT WITH SOUND AND PRUDENT BUSINESS PRACTICES, WHILE MAINTAINING A HIGH LEVEL OF FINANCIAL STABILITY AND CREDIT. THE DISTRICT HAS INITIATED OPTIONAL RATE-RELATED CONSERVATION PROGRAMS SUCH AS TIME-OF-USE RATES AND AIR CONDITIONER LOAD MANAGEMENT RATES FOR RESIDENTIAL CUSTOMERS, TIME-OF-USE RATES, AND AUXILIARY POWER AND CURTAILABLE RATE PILOT PROGRAMS FOR COMMERCIAL/INDUSTRIAL CUSTOMERS. THESE PROGRAMS ENABLE CUSTOMERS TO SAVE MONEY ON THEIR BILLS AS A RESULT OF SHIFTING ENERGY FROM THE PEAK PERIOD.

THE LOCALLY-ELECTED BOARD OF DIRECTORS HAS BEEN SENSITIVE TO THE GROWING NUMBER OF RATE INCREASES AND THE INCREASING RATE LEVELS ON RESIDENTIAL CUSTOMERS AND THEREFORE, EFFECTIVE OCTOBER 1, 1987, THE BOARD INSTITUTED RESIDENTIAL BASELINE RATES. THESE BASELINE RATES WERE IMPLEMENTED TO PROVIDE A QUANTITY OF ELECTRICITY AT AFFORDABLE RATES FOR LOW-USE RESIDENTIAL CUSTOMERS. SO NOW FOR THE FIRST TIME, SMUD RESIDENTIAL CUSTOMERS PAY A LOWER RATE FOR A BASELINE QUANTITY OF ELECTRICITY AND A HIGHER RATE FOR ADDITIONAL AMOUNTS.

RATE ADVISORY COMMITTEE

THE BOARD OF DIRECTORS HAS RECOGNIZED PROBLEMS WITH THE DISTRICT'S RATE STRUCTURE AND RATE SETTING PROCESS AND HAS APPOINTED A RATES ADVISORY GROUP COMPOSED OF 10 COMMUNITY REPRESENTATIVES TO REVIEW AND EVALUATE THE DISTRICT'S RATE STRUCTURE AND RATEMAKING PROCESS. THE MEMBERS OF THE GROUP REPRESENT RESIDENTIAL, AGRICULTURAL AND COMMERCIAL/INDUSTRIAL CLASSES OF CUSTOMERS. SPECIFICALLY, THE ADVISORY GROUP IS CHARGED WITH TWO FUNCTIONS:

1. THE DEVELOPMENT OF A PUBLIC HEARING PROCESS WHICH FACILITATES PUBLIC INPUT AND COMPILES A USEFUL RECORD FOR ULTIMATE DECISION MAKING.
2. THE DEVELOPMENT OF A PROPOSED RATE STRUCTURE BY IDENTIFYING RATE POLICIES TO BE ADDRESSED BY THE BOARD.

HAVING MET FREQUENTLY SINCE JULY 1987, THE ADVISORY GROUP HAS RECENTLY REVIEWED THE CURRENT RATE SETTING PROCESS AND ALTERNATIVE PROCESSES. THE CONSENSUS OF THE ADVISORY GROUP IS THAT A COMBINATION OF RULEMAKING PROCEEDINGS WITH COMMUNITY WORKSHOPS MAY BE MOST APPROPRIATE TO SUPPLEMENT THE DISTRICT'S CURRENT PROCESS. OVER THE COMING MONTHS, THE ADVISORY GROUP WILL CONTINUE TO WORK CLOSELY WITH THE STAFF AND BOARD OF DIRECTORS TO IDENTIFY WAYS TO FACILITATE GREATER INFORMED PUBLIC PARTICIPATION IN THE RATE SETTING PROCESS.

CONCLUSION

IN CONCLUSION, LET ME SAY, THE DISTRICT IS WELL ON ITS WAY TO RESOLVING ITS RESOURCE NEEDS, INCLUDING THE FUTURE ROLE OF RANCHO SECO AND IS EXAMINING ITS RATE STRUCTURE AND RATE PROCESS WITH MAJOR COMMUNITY PARTICIPATION.

COMMENTS OF FRANK HAHN
DEPUTY GENERAL MANAGER
SACRAMENTO MUNICIPAL UTILITY DISTRICT

FOR THE
ASSEMBLY COMMITTEE ON UTILITIES AND COMMERCE
HONORABLE GWEN MOORE, CHAIRWOMAN

INTERIM HEARING ON
PROPOSED CONSOLIDATION OF SMUD AND PG&E
OCTOBER 6, 1987

FRANK HAHN TESTIMONY

RESOURCE AND TRANSMISSION OPTIONS

THE DISTRICT WILL HAVE TO DEVELOP BETWEEN 500 MW AND 1400 MW OF NEW RESOURCES BY 1990, DEPENDING ON THE STATUS OF RANCHO SECO, THAT IS WHETHER WE DIVEST, OPERATE, REPOWER OR TERMINATE. IN ADDITION, GROWTH IN SACRAMENTO WILL REQUIRE APPROXIMATELY 50 MW OF NEW RESOURCES TO BE DEVELOPED EACH YEAR THROUGH THE '90'S.

OPTIONS AVAILABLE TO FILL THESE NEEDS INCLUDE 100 MW FROM THE FEDERAL GOVERNMENT'S WESTERN AREA POWER ADMINISTRATION (CENTRAL VALLEY PROJECT); 200 MW OF POWER PURCHASES FROM THE NORTHWEST OVER SMUD'S EXISTING INTERTIE RIGHTS; A 50 MW COGENERATION PROJECT BEING DEVELOPED IN PARTNERSHIP WITH CAMPBELL SOUP COMPANY, APPROXIMATELY 100 MW OF NEW LOAD MANAGEMENT AND CONSERVATION BEYOND THAT ALREADY INCLUDED IN THE DISTRICT'S PLANS; AND A 200 MW ENERGY STORAGE PROJECT, WHICH IS COFUNDED BY THE DISTRICT, THE CALIFORNIA ENERGY COMMISSION, AND THE ELECTRIC POWER RESEARCH INSTITUTE.

THE RFP PROCESS, RECENTLY COMPLETED, TURNED UP MANY OFFERS FOR POWER PURCHASES. MOST OF THE POWER AVAILABLE IS AVAILABLE ONLY AT HIGH COST. THOSE OFFERS WHICH DID PROPOSE COMPETITIVE RATES, CANNOT BE DELIVERED IN SACRAMENTO EXCEPT OVER THE PG&E TRANSMISSION SYSTEM.

THE DISTRICT IS DEVELOPING TWO MAJOR TRANSMISSION PROJECTS FOR THE FUTURE. THE CALIFORNIA-OREGON TRANSMISSION PROJECT (COTP), WHICH INCLUDES 200 MW OF DISTRICT OWNERSHIP, WILL PROVIDE ACCESS TO THE NORTHWEST ENERGY SOURCES, WHICH ARE EXPECTED TO BE AVAILABLE INDEFINITELY. THE SMUD-SIERRA PACIFIC INTERTIE PROJECT (SSIP) WILL TIE SACRAMENTO TO RENO AND THE TRANSMISSION LINES ACROSS NEVADA TO THE COAL FIELDS TO UTAH AND MONTANA. ENERGY SURPLUSES GENERATED IN THESE AREAS ARE EXPECTED TO BE AVAILABLE FOR MANY YEARS. NEITHER OF THESE LINES HAS BEEN COMPLETED AND BOTH MUST SATISFY ENVIRONMENTAL AND LOCAL CONCERNS. TRANSMISSION ACCESS TO FUTURE LOW COST ENERGY PURCHASES IS CERTAINLY THE SINGLE MOST IMPORTANT ELEMENT OF THE DISTRICT'S LONG RANGE STRATEGY.

WHILE THE DISTRICT IS NEGOTIATING WITH PG&E FOR POWER PURCHASES WE ARE ALSO ATTEMPTING TO SECURE ACCESS THROUGH THE PG&E SYSTEM FOR COMPETING POWER PURCHASES. THIS TRANSMISSION ACCESS IS NOT AVAILABLE AND PG&E IS ATTEMPTING TO INCREASE THE PRICE OF TRANSMISSION WHEELING, INDEPENDENT OF THE COST OF PROVIDING TRANSMISSION SERVICES.

CLEARLY, THE DISTRICT CAN HAVE RESOURCES AVAILABLE TO MEET FUTURE CUSTOMER NEEDS. IN ORDER FOR THE DISTRICT TO SELECT THE MOST ECONOMICAL OPTIONS FOR FUTURE DEVELOPMENT, TRANSMISSION ACCESS IS ESSENTIAL. THIS TRANSMISSION ACCESS WILL INCLUDE THE USE OF THE TWO PROPOSED LINES, AND WHEELING OVER THE PG&E TRANSMISSION SYSTEM.

COMMENTS OF GERALD L. JORDAN

Executive Director

CALIFORNIA MUNICIPAL UTILITIES ASSOCIATION

INTERIM HEARING OF THE

ASSEMBLY UTILITIES AND COMMERCE COMMITTEE

Honorable Gwen Moore, Chairwoman

on

PROPOSED SMUD & PGE CONSOLIDATION

October 6, 1987

Chairwoman Moore, members of the Committee, I am Jerry Jordan, Executive Director of the California Municipal Utilities Association, a statewide organization of publicly owned water, gas and electric utilities. Thank you for the opportunity to present our views on the so called "consolidation" of PG&E and SMUD. Let us be very clear. The PG&E proposal is a hostile attempt to take over a 40 year old competitor of PG&E and is a characteristic example of the anti-competitive and predatory practices of PG&E.

The question with which this committee should concern itself is not only will the SMUD customers benefit in the long run (they will not) but will the PG&E ratepayers and the state as a whole benefit over the long run? The answer is no. The sole beneficiary would be PG&E stockholders.

The PG&E proposal has two main features. One is the decommissioning of Rancho Seco and the other is the freezing of rates in the SMUD service territory for some unspecified period of time. These are mutually exclusive propositions. How can the PUC, or indeed the Legislature, allow PG&E's current ratepayers to pay the cost of decommissioning Rancho Seco especially in light of the fact that the Sacramento voters could decide next June to close the plant down and bear the costs themselves? And if Sacramento ratepayers are to pay the costs of dismantling Rancho Seco then how can rates be frozen. It would clearly be unfair anyway to freeze one geographical area's rates in preference over other areas. PG&E ratepayers not wishing to subsidize other areas should be very opposed to this so called "consolidation".

There are only two possible reasons that PG&E is willing to make the offer to freeze rates for some unknown period. One is the very real probability that the PUC will perform its constitutional responsibility and prohibit geographical rate discrimination. The other is that PG&E fully expects to recover in future rates anything it loses during the freeze.

It does not take a Ph.D. economist to know that the economics of the PG&E proposal does not work for anyone but the PG&E investor. First the SMUD board would be derelict in its responsibility to the voters which elected them if it

agreed to sell the SMUD system at anything less than full market value. PG&E would then have to finance the acquisition at current market rates with taxable financing (the non-taxable bonds of SMUD would have to be repaid). Since much of the system has already been paid for by SMUD ratepayers the resultant cost of serving the Sacramento area would have to rise dramatically. In addition to the increased cost of refinancing the capital facilities, PG&E would retire Rancho Seco and pay the decommissioning costs. PG&E then proposes to supply energy to Sacramento from the very troubled Diablo Canyon plant which is more expensive to produce energy from than a rebuilt Rancho Seco. Added to those increased costs PG&E claims they will pay \$15 million in local taxes. And of course added to all of this is the profit which must be paid to PG&E's investors. These increased costs have to add up to significant rate increases in the Sacramento area after the so called "freeze" has thawed out.

In addition PG&E has been complaining that Public Utilities Regulatory Policies Act (PURPA) contracts it has been forced to sign will cost it in excess of \$2billion in unneeded power. Those costs also would be spread to Sacramento. In fact it is Sacramento's growing market which attracts PG&E because it will help PG&E to get rid of its excess, a process known as dumping. Sacramento should not be forced to pay for PG&E's dumping.

If the above economics were not sufficient reason to reject the PG&E "offer" think of what will happen if PG&E is successful in getting all of the Diablo Canyon costs in their rate base. The above costs to Sacramento will be further increased because of the increased rate base.

The implication in the PG&E offer is that PG&E because of its size is better managed and therefore more efficient. The Committee would do well to ask the ratepayers in other areas of the PG&E service territory if they are comfortable with the efficiency of PG&E. The PG&E claim to management prowess does not hold up to the record it has had with Diablo Canyon. The problems experienced there (a project which was on the drawing boards long before Rancho Seco) are well known. Suffice it to say that the PUC staff has recommended that \$4.65 billion of the \$5.8 billion cost of the plant not be allowed in the PG&E

rate base and that the Attorney General's office has asked for an immediate ruling from the administrative law judge that at least \$2.5 billion not be allowed in the rates because of mismanagement. In addition it would seem obvious that a plant as troubled as Diablo Canyon could well experience in the future the types of problems that Rancho Seco is now getting over.

What implications would those problems have for PG&E rates and for a SMUDless Sacramento. PG&E would like everyone to believe that because they are bigger they are better. The record of the last 40 years does not prove that. For at least 38 of those 40 years SMUD rates were much lower than PG&E's, and in spite of the current problems SMUD rates have just now reached the level of PG&E and in some customer classes remain significantly lower. The real desire of PG&E is to eliminate its number one competitor in Northern California. We would not expect PG&E to stop there. If PG&E is successful in eliminating its biggest competitor we believe it will its their anti-competitive practices on all other publicly owned utilities in Northern California. It is no secret that 60 of PG&E's 100 largest electric customers have left the PG&E system for other options. Some have decided on producing their own electricity and others have moved to municipal utility service territories including SMUD.

As the committee is well aware SMUD has sent out an RFP for the supply of power and has received a huge response from parties interested in providing power. There is a catch however. The catch is that PG&E controls the transmission in and out of the Sacramento and in fact the Northern California area. That in and of itself is an anti competitive practice. PG&E continues to try to use its transmission system to control the growth and independence of publicly owned utilities.

Publicly owned utilities in Northern California are cooperating in an attempt to build a 230kv transmission line from the Geysers Area to connect with Western Area Power Administration's line near Williams, California. This project, the Geothermal Public Power Line, was a requirement of the NCPA interconnection agreement with PG&E imposed by PG&E in the contract. PG&E has opposed the line at the Energy Commission and has tried to force the line to be connected to the PG&E system in the Vacaville/Dixon area. PG&E is now favoring

an upgrade of its current transmission line in opposition to the GPPL line. PG&E is even attempting to force the publicly owned utilities to pay for the upgrade of its system without reducing the wheeling costs associated with the line.

PG&E has also been vigorously opposing a short extension of a Western Area Power Administration transmission line to serve the federal government at the Lawrence Livermore Lab.

PG&E is participating along with publicly owned utilities in California in the California Oregon Transmission Project (COTP), or the third North West Intertie, but it has been obvious that PG&E's only interest in participating is in maintaining some degree of control over transmission access. It has become obvious that the public agencies will proceed with the line, with or without PG&E's involvement.

It should also be noticed by the committee that PG&E has actively been seeking legislation and Energy Commission regulation changes to eliminate competition from small power producers. They have sought legislation designed to eliminate PURPA contracts already signed and have lobbied the Energy Commission to increase its jurisdiction over smaller and smaller plants in order to eliminate the competition posed by those plants.

The concern of the legislature should be directed to the lack of control of predatory practices of investor owned utilities. PG&E is clearly attempting to eliminate its largest competitor in California and to provide a captive market to help pay for PG&E's past management mistakes and over building. Investor owned utilities are afraid of competition. Evidence the attempts at last second legislation by Southern California Edison to prevent the City of Southgate from establishing a municipal utility. The legislature should consider the following:

1. Any public agency is at a severe disadvantage in dealing with a takeover attempt by an investor owned utility. State law prohibits public agencies from spending money to influence a ballot measure. Investor owned utilities are not currently subject to this restriction. The legislature should consider legislation prohibiting investor owned utilities from spending money designed to convince voters to approve the takeover.

2. There is currently no antitrust review at the state level of takeover attempts by corporations of public agencies. Perhaps the Attorney General should be required to review the anti competitive practices involving corporate attempts to acquire public agencies.

3. The Public Utilities Commission should be prohibited from allowing the costs of decommissioning Rancho Seco from being paid by current PG&E ratepayers.

4. The PUC should be directed to prohibit any geographical subsidies.

5. The PUC should be directed to prohibit any rate subsidy resulting from a takeover from being paid by either the current PG&E ratepayers or from being recovered in the future from the ratepayers acquired. I.E. any subsidy should have to come from investors.

6. Wheeling-investor owned utilities should be required to allow their transmission to be upgraded at the proponents expense if there is insufficient capacity to wheel for anyone requesting wheeling.

COMMENTS OF GORDON W. HOYT
PUBLIC UTILITIES GENERAL MANAGER
CITY OF ANAHEIM, CALIFORNIA

Interim Hearing of
The Assembly Utilities and Commerce Committee

Honorable Gwen Moore, Chairwoman
on
Proposed SMUD and PG&E Consolidation
October 6, 1987

My name is Gordon W. Hoyt. I am general manager of the Public Utilities Department of the City of Anaheim. I am a former president of both the California Municipal Utilities Association and the American Public Power Association. I appreciate this opportunity to appear before you today.

The purpose of my comments is to describe the importance of competition between investor-owned utilities such as Pacific Gas and Electric Company ("PG&E") and publicly-owned systems such as Sacramento Municipal Utility District ("SMUD"), and how, as a result of that competition, California has a more economic and reliable electric power supply.

The electric utility industry in this country is controlled to a great extent by large investor-owned utilities such as PG&E and Southern California Edison Company ("SCE"). Since 1920, private utilities have, through mergers and consolidation, centralized their economic power. In 1920, there were about 4,000 private electric companies. There are only about 200 operating today. These companies have vast generating and transmission resources.

In contrast, there are more than 2,200 publicly owned utilities. Most are much smaller than the private utilities, and many have no generating capacity of their own. The total generating capacity of municipally owned utilities is only a small fraction of that of the private companies.

Despite having much more limited resources, consumer-owned electric systems play an important competitive role in the industry. Put in the most basic terms, publicly-owned systems provide alternatives to investor-owned companies. The existence of publicly-owned systems demonstrates that customers who are dissatisfied with the performance of a privately-owned utility have the possibility of establishing a consumer-owned system instead. We provide a competitive "yardstick" against which the performance of the private monopolies can be measured, and as a manager of PG&E's East Bay Division conceded, public entities force the private companies to operate more efficiently and economically.

"This [competition from municipally owned utilities] is real tough competition. It is a threat. The only way we can combat it is to increase the efficiency of our operation and to provide our customers with the best possible utility service."

Why are the private utilities constantly looking over their shoulders at the performance of the neighboring publics?

The reason is simple. Public utility regulators are able to use the performance of publicly owned utilities to help determine the legitimacy of rate increases sought by the private companies. Even more importantly, however, private utilities know that a viable public sector gives their ratepayers a real alternative to which to turn if the private utility's performance is inadequate.

Publicly-owned systems generally face significant disadvantages in their efforts to compete with investor-owned companies. PG&E's total generating capacity exceeds 18,680 megawatts. In 1986, PG&E's gross revenues totalled \$7.8 billion, and its total assets exceed \$21 billion. Similarly, Southern California Edison has total capacity resources of 18,300 megawatts. Edison made profits of \$768 million in 1986 on gross revenues of \$5.3 billion. Its assets total over \$13.2 billion.

Competing against these two private giants in California is a diverse group of publicly-owned utilities which, except for SMUD and the Los Angeles Department of Water and Power, have limited generating resources and no independent major transmission facilities.

Anaheim, which has one of the oldest municipally-owned systems in California, sells electricity to approximately 95,000 customers located in an approximately 45 square-mile service territory. Until recently Anaheim was totally dependent upon Southern California Edison for its electric power supply requirements. We found ourselves faced with the fact that Edison was continually putting Anaheim and its other resale customers in a "price squeeze" in which the rates Edison charged them for power at wholesale exceeded the rates Edison was charging for similar service at retail. We determined that Anaheim could not continue to remain a competitively viable entity under those circumstances. Thus Anaheim took steps to develop its own independent power supply. We presently have ownership interests in the San Onofre Nuclear Generating Station Units 2 and 3 and the Intermountain Power Project. We also receive an allocation of power from the Hoover Dam and have entered into agreements with other utilities for the purchase of energy and capacity.

This independence, it should be noted, has not come inexpensively for Anaheim's citizens. By an overwhelming majority, the citizens have voted to participate in projects financed for over \$1 billion--or over \$4,000 for every man, woman and child in the city--for interests in new generating and transmission resources that will help Anaheim to break free from the kind of high electricity prices experienced in the

past. In this way the citizens are hoping to get control over their power supply and reduce dependence on SCE. Anaheim's efforts to meet its own power supply needs have helped to reduce the cost of electric capacity and energy in Southern California and increased overall electric reliability to the region. By undertaking the responsibility to obtain the resources needed to meet its power supply requirements, Anaheim has reduced the need for Edison to plan for and finance that additional amount of new generating resources. This results in lower costs for Edison's customers.

Other publicly-owned systems in California including SMUD have taken similar steps to become more resource independent from PG&E and Edison. As with Anaheim, these utilities have helped to provide more low cost power with greater reliability, which benefits not only their own citizen customers but everyone in the state.

However, contrary to the statement of the PG&E representative quoted earlier, privately-owned companies have not limited their response to competition from publicly-owned systems to simply improving their efficiency and quality of service. In addition to such legitimate competitive responses, the private utilities have consistently abused their monopolistic status and have attempted either to eliminate or cripple their consumer-owned competitors.

The private utilities have repeatedly denied consumer-owned utilities like Anaheim access to transmission facilities, thereby denying us the opportunity to obtain lower-cost power from alternate sources. The California private utilities have refused to cooperate in, and indeed have actively interfered with, the development of independent, consumer-owned utility systems, however small. For a current example of such interference one only has to examine the conduct of SCE in thwarting the efforts of the City of Southgate to form a municipal electric utility during the summer of 1987. The experience of Anaheim and other Southern California cities with which I am closely familiar, has, to say the least, been frustrating. Anaheim has had to initiate and pursue legal actions, including an antitrust suit against Edison in federal district court and a separate, federal proceeding against the private utilities in California before FERC in order to gain access to alternative power sources and transmission lines.

Similarly, whenever we have tried to purchase low cost electric energy from the Pacific Northwest, we have found our access limited by the private utilities controlling transmission service over the Pacific Northwest-Southwest

Intertie facilities. We executed a contract with the Bonneville Power Administration ("BPA") for the purchase of both surplus and provisional energy; then we entered into a contract with the State of California, under which it assigned a portion of its rights to transmission over the Intertie facilities to Anaheim. Edison and PG&E, however, refused to permit transmission services. Edison also refused to provide firm transmission over its share of the Intertie. As a result, we have been unable to make any significant purchases of inexpensive power from BPA.

Despite the roadblocks thrown up by the privately-owned companies, publicly-owned utilities have made a tremendous contribution toward assuring a reliable and economic supply of power for the people of California. As I mentioned before, Anaheim, along with other publicly-owned systems, has taken substantial responsibility for financing such projects as the Intermountain Power Project and San Onofre Nuclear Generating Station Units 2 and 3. We, along with Riverside, entered into an innovative contract with Nevada Power Company to purchase interruptible energy which was surplus to Nevada Power's needs and economically advantageous for our customers. We have purchased low-cost economy energy from other sources as well, and we and other publicly-owned systems are constantly on the lookout for opportunities to bring into California lower cost power supplies whenever we can get transmission from the private companies.

Anaheim and many other publicly-owned systems are participating in plans to increase transmission capacity to bring in low cost power from the Pacific Northwest by adding a third AC line to the Pacific Intertie. Furthermore, although only a limited number of publicly-owned systems were permitted to participate in the existing Intertie facilities, the Intertie probably would not have been built by the private utilities if there had not been significant competitive pressure from publicly-owned systems and the federal government.

Anaheim, along with Azusa, Banning, Colton, Riverside, SMUD and the Northern California Power Agency filed a joint license application at the Federal Energy Regulatory Commission seeking to obtain licenses to operate the Cresta-Rock Creek and Haas-Kings River hydroelectric facilities, which currently are held by PG&E. In filing competing license applications the publicly-owned systems submitted proposals to increase the generating capacity of the hydro-electric facilities. PG&E responded by amending its plans to match those of the public systems. While Congress subsequently amended the Federal Power Act so as to eliminate the public systems as license competitors, the fact remains that California will benefit from increased hydro-electric capacity which would not have been available but for the competition between publicly and privately-owned systems.

Another advantage of the competition between public and private systems is the opportunity for capacity and energy transactions between various utilities. Anaheim can reduce its power costs by entering into transactions with other utilities which may have surplus capacity and energy to sell or may need to purchase such capacity and energy. If the number of utilities is reduced by take over or mergers the marketplace is made smaller and transaction opportunities are limited.

Both courts and regulatory agencies have recognized the benefits of competition in the electric utility industry and have acted to prevent efforts by investor-owned utilities to increase their market power at the expense of consumer-owned systems. Federal courts have enforced antitrust laws to prohibit investor-owned utilities from using their strategic dominance over transmission facilities and sources of power to foreclose or inhibit competition from publicly-owned systems. The Nuclear Regulatory Commission has required utilities seeking licenses for nuclear plants, including SCE and PG&E to provide access to those plants and necessary transmission facilities to publicly-owned systems in their areas. The Federal Energy Regulatory Commission ("FERC") is required to consider the effects of proposed wholesale rate increases on competition between the utility seeking the increase and its wholesale customers. Most recently, in a draft order approved at its meeting of September 23, 1987, in a case involving SCE and its wholesale customers, including Anaheim, the FERC emphasized its concern with rate relationships which cause or are likely to cause increased concentration of economic power at the expense of a utility's competitors or to discourage entry into the market. The benefits of competition between investor-owned utilities and publicly-owned systems are widely recognized in the formulation and implementation of antitrust and regulatory policy.

The benefits of competitive pressures work in both directions. The existence of publicly-owned systems as visible alternatives encourages private companies to operate more efficiently and to attempt to hold down their rates. At the same time, the need to compete effectively with the private utilities has compelled publicly-owned systems to devote their innovative skills and resources, both human and economic, to acquiring power supplies at the lowest possible cost. The beneficiaries of the competitive tension between publicly and privately-owned systems have been all of the customers of both kinds of systems, and all customers will suffer if that competition is diminished.

REMARKS BEFORE THE STATE ASSEMBLY UTILITIES AND COMMERCE COMMITTEE
INFORMATIONAL HEARING ON THE PROPOSAL BY PG&E TO BUY SMUD

October 6, 1987

David G. Coleman, Western Area Power Administration

My name is David G. Coleman, Area Manager for Western Area Power Administration's (Western) Sacramento Area Office. I am pleased to be able to present information for your Assembly committee regarding Western's power marketing activities here in California associated with the Sacramento Municipal Utility District (SMUD).

Western, as a part of the Department of Energy, and headquartered in Golden, Colorado, markets hydroelectric power from 49 powerplants operated by the Bureau of Reclamation, the U.S. Army Corps of Engineers, and the International Boundary and Water Commission. Current maximum operating capacity is more than 9,500 megawatts. It also markets 500 MWs of coal-fired generation located near Page, Arizona.

Western's service area covers 1.3 million square miles. Western's wholesale power customers provide service to millions of consumers in 15 western states. In addition to the Headquarters Office in Golden, five Area Offices are located in Billings, Montana; Boulder City, Nevada; Loveland, Colorado; Salt Lake City, Utah, and here in Sacramento, California.

Last year, Western

- o supplied hydroelectric power to more than 570 wholesale power customers.
- o operated and maintained more than 16,200 miles of transmission lines, 240 substations and other related facilities.
- o sold more than 45 billion kilowatthours (kWh) of power, enough to serve about 6 million households or approximately 19 million people for one year.
- o generated nearly \$615 million in power revenues.

Two of Western's regional offices, referred to as Area Offices, serve the state of California. Our Boulder City, Nevada, Area Office serves southern California as well as southern Nevada and Arizona. Power produced from the hydroelectric system on the Colorado River is the primary source of Federal power serving southern California. The Sacramento Area Office serves the northern and central portions of California and Nevada. The primary source of power is from the Central Valley Project (CVP), constructed and operated by the Bureau of Reclamation.

In addition to the installed generating capacity of 1800 MW from the CVP, Western also has a 400 MW entitlement on the Pacific Northwest/Southwest intertie and has been importing power from the Northwest to serve its California loads since the mid-1960's. This supplemental power purchased from the Northwest is required to meet the contractual obligations of the Federal

marketing program in California. Approximately 3000 gigawatt hours are imported annually into California by the Federal Government to serve the Sacramento Area Office customers.

Our primary transmission system extends from the Redding, California area to Tracy in central California. With the exception of seven direct-connected customers, Western relies upon the PGandE transmission system to deliver its power from our main transmission system to its preference customers. Contracts for the firming and wheeling of CVP power with PGandE are in effect until 2004.

Approximately 1400 MW of power is sold as wholesale power to over 80 preference customers located in California and western Nevada. In addition, surplus power excess to preference customers' needs is marketed to the Pacific Gas and Electric Company (PGandE). The two largest CVP customers are SMUD and PGandE.

With respect to your specific agenda items, I will limit my comments to Western's relationship and allocation of Federal power to SMUD and to those transmission planning and construction activities which pertain to Western's services to SMUD. The Federal Government (first the U.S. Bureau of Reclamation, then since 1977, Western) has been serving cost-based wholesale power to preference customers in northern and central California since the early 1950's when the initial features of the CVP were completed and began to be fully operational. SMUD is one of those preference customers under Federal reclamation law. The law requires that Western give preference in the

allocation of Federal power to municipalities and other public corporations and agencies, and also to cooperatives and other nonprofit organizations financed in whole or in part by loans made pursuant to the Rural Electrification Act of 1936. SMUD began operations in 1946, and received its first allocation of Federal CVP power in 1952. In 1954, SMUD established a direct connection with the CVP transmission system.

Through the years, the allocation of Federal power to SMUD has grown and at the present time SMUD has an allocation of 360 MW. This is about 25 percent of the CVP power available for commercial sale. Coincidentally, this power also represents about 20 to 25 percent of SMUD's annual load. Our contract with SMUD extends to the year 2004, and SMUD also has a contractual right to a proportion of available CVP power from 2005 through 2014, the amount, terms and conditions to be determined.

As with any of the contracts Western has with its preference customers, SMUD's contract with Western cannot be assigned to any other party without Western's written approval. This approval for assignment cannot be granted if it results in violation of reclamation law. Western will carefully review any SMUD/PGandE proposal to determine the effect of the proposal on SMUD's present status as a preference customer. If SMUD should cease to be a preference customer as a result of any merger or consolidation, it will no longer be eligible for an allocation of Federal Power. At that time Western would make a determination as to what to do with the 360 MW of power.

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Regarding transmission access and purchase of power resources from the Northwest, the Sacramento Area Office of Western imports both firm and non-firm power over its 400 MW share of the existing AC transmission lines. Since 1970 approximately 80 percent of all power purchased by Western from the Northwest has been acquired through an agreement with the owners of the Centralia, Washington, coal-fired steam plant or the Bonneville Power Administration (BPA). Other suppliers include entities such as British Columbia Hydro, City of Tacoma, Longview Fibre Corporation, and Basin Electric Power Cooperative. As a general rule, Western has looked to the Northwest for the purchasing of surplus power because these purchases have been more economical in recent years than to construct new projects ourselves or to purchase from other suppliers in the state of California. We anticipate that the Northwest will continue to have surplus power at favorable rates so as to assure a continued power resource to meet our supplemental contractual needs. We also believe that it will be important for California to continue to upgrade its transmission system internally and those high voltage lines leading to the generating sources in other states.

One project which is currently in varying stages of planning and design is the California-Oregon Transmission Project. There are 31 participants in California who are involved in this project. Western will be upgrading a portion of its 230-kV system to 500-kV, using non-Federal funding, as its contribution to the success of this project. I am sure that you will be hearing more about this project and participation by entities and from my colleague from BPA. We believe that the state of California should continue to support the construction of this Third AC line as well as other transmission projects that will facilitate the most efficient use of resources throughout the Western states.

BEFORE THE ASSEMBLY COMMITTEE ON UTILITIES AND COMMERCE

CALIFORNIA LEGISLATURE

OCTOBER 6, 1987

BPA'S OFFER TO SACRAMENTO MUNICIPAL UTILITY DISTRICT

JAMES J. JURA

ADMINISTRATOR

BONNEVILLE POWER ADMINISTRATION

Thank you for being provided the opportunity to speak with you about BPA's proposal to sell power to the District. BPA carefully considered SMUD's Request for Proposal for Electric Power Resources and developed three proposals designed to meet SMUD's needs. These proposals are based on an assessment of BPA's strengths in the bulk power supply market and the constraints which make it difficult for BPA to meet the District's needs. I will begin by describing the assessment of these strengths and constraints and conclude with a description of our proposals.

BPA's Strengths

BPA is a low cost supplier with a large surplus of capacity and energy. BPA's pricing can provide the District price predictability. Also BPA is prepared to enter into long-term agreements to provide power as long as it is surplus to the needs of Northwest utilities.

BPA is prepared to sell power delivered to the California/Oregon border at a price which starts at approximately 30 mills/kWh. It is our understanding that this price is approximately 25 percent below the District's alternative cost. I believe that the purchase of power from BPA could represent a significant reduction in cost for the District's ratepayers.

As I will describe later, BPA is constrained to only sell power which is surplus to the needs of Northwest utilities. I want to stress, however, that currently, BPA has over 1000 avg. MW of surplus energy and over 2000 MW of surplus capacity. Different forecasts developed by the Northwest Power Planning Council and BPA come to the same conclusion. That is BPA's energy surplus is likely to last through the late 1990's and the capacity surplus is expected to last well into the next century. Attached to this statement is BPA's forecast of our capacity and energy surpluses.

Because there are concerns in the Northwest about selling resources which might otherwise be used in the region, BPA has limited the amount of power it will sell to extraregional utilities. Even with these limitations BPA is willing to enter into agreements to sell up to 725 avg. MW of energy and up to 1350 MW of capacity to utilities outside the Pacific Northwest. BPA would propose that such agreements could be structured to last up to 20 years.

In short, BPA believes that it can provide the District with a low cost source of power which can be beneficial for the District's ratepayers for well into the future.

Constraints on a Purchase from BPA

There are three constraints which impact a large sale of power from BPA to SMUD:

1. Transmission access in Northern California
2. Statutory requirements that BPA assure all power sold outside the Northwest is surplus to the needs of the Northwest.
3. SMUD's needs to provide reserves for any large amounts of purchased power.

I will discuss each of these individually.

Transmission Constraints

There is currently approximately 5200 MW of intertie capacity between the Pacific Northwest and California. BPA has rights to approximately 80 percent of the northern portion of the intertie. Consequently, BPA has the transmission capability to deliver large amounts of power to the California/Oregon border.

South of the California/Oregon border, rights to the intertie are shared by a variety of parties. It is BPA's understanding that SMUD has limited access to intertie capacity from the California/Oregon border to the SMUD system. BPA has assumed that SMUD's capability to receive power delivered to the border is currently limited to approximately 100 MW. Upon completion of the California/Oregon Transmission Project SMUD will obtain additional transmission capacity. Consequently, a direct purchase by the District from BPA would be limited to approximately 100 MW until the COTP is completed and up to 300 MW thereafter. Purchases from BPA, or other Northwest suppliers which exceed these amounts would require the cooperation of other intertie owners in California.

Regional Preference

In 1964 the Congress provided the legislative authorization for construction of the Pacific Northwest/Pacific Southwest intertie. The original authorization of the intertie was based on the assumption that BPA would only sell power that is surplus to Northwest needs. A provision was included in the legislation to assure that BPA would not sell the resources located in the Northwest, leaving the Northwest to have to find imports to serve its needs. This legislative statute requires that BPA include what has been termed callback provisions in any contract with an extraregional utility. The callback provisions provide that BPA can terminate the sale of energy on 60 days notice and the sale of capacity on 60 months notice if the power is needed to serve Northwest loads.

It is important to note that the callback provisions do not apply to capacity/energy exchanges. For this reason BPA has structured sales to California utilities which provide for the sale of energy until BPA's surplus is exhausted. At that point the sale would convert to a capacity/energy exchange. This type of arrangement matches BPA's system which is primarily energy constrained with that of California utilities which tend to be capacity constrained.

Reserves

Finally, BPA recognizes that SMUD has limited connections to the BPA system. Consequently, a line outage could cause severe problems. The provision of reserves would be necessary and becomes more important the larger the purchase from BPA.

BPA's Proposal

Recognizing these strengths and constraints BPA has developed three proposals to meet the District's needs. These three proposals include:

- To enter into negotiations to sell SMUD power equivalent to its existing transmission capacity. BPA would sell energy as long as there is a surplus. Upon reaching load/resource balance the sale would convert to a capacity/energy exchange.

- To enter into negotiations for the sale of additional amounts of power under the same conditions as those noted above. This sale would become effective upon completion of the California/Oregon Transmission Project.

- To enter into negotiations with PG&E and the District designed to develop a joint venture proposal combining PG&E's resources with BPA's. Such a proposal would be designed to provide benefits to PG&E, BPA and the District. BPA has written to PG&E asking about their interest in pursuing such a proposal. PG&E has responded that it is willing to evaluate any proposal put forward by BPA.

Conclusion

BPA believes that a power purchase by SMUD from BPA could benefit ratepayers of both entities. Consequently, BPA is prepared to enter into negotiations which would lead to a sale of power up to the amount of transmission capacity available to SMUD. I am encouraged by the District's positive reaction to our proposal and we look forward to initiating discussions with you.

BPA, however, is also prepared to sell additional amounts of power. A larger sale would likely require the assistance of PG&E. BPA plans to pursue discussions to determine if such an arrangement can be developed.

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Figure 7
FEDERAL FIRM CAPACITY SURPLUS
Capacity Available For A 50-Hour/Week Sale

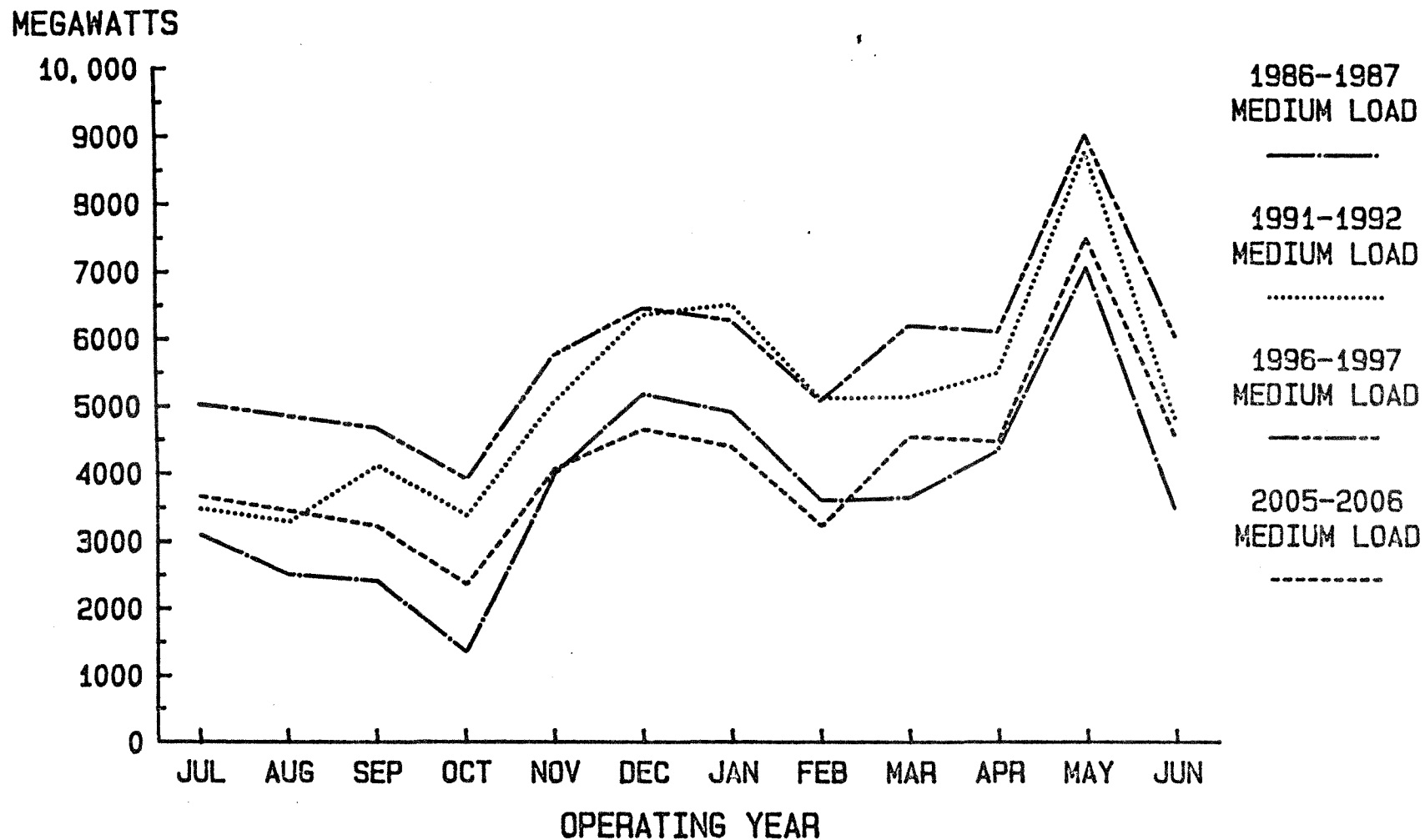
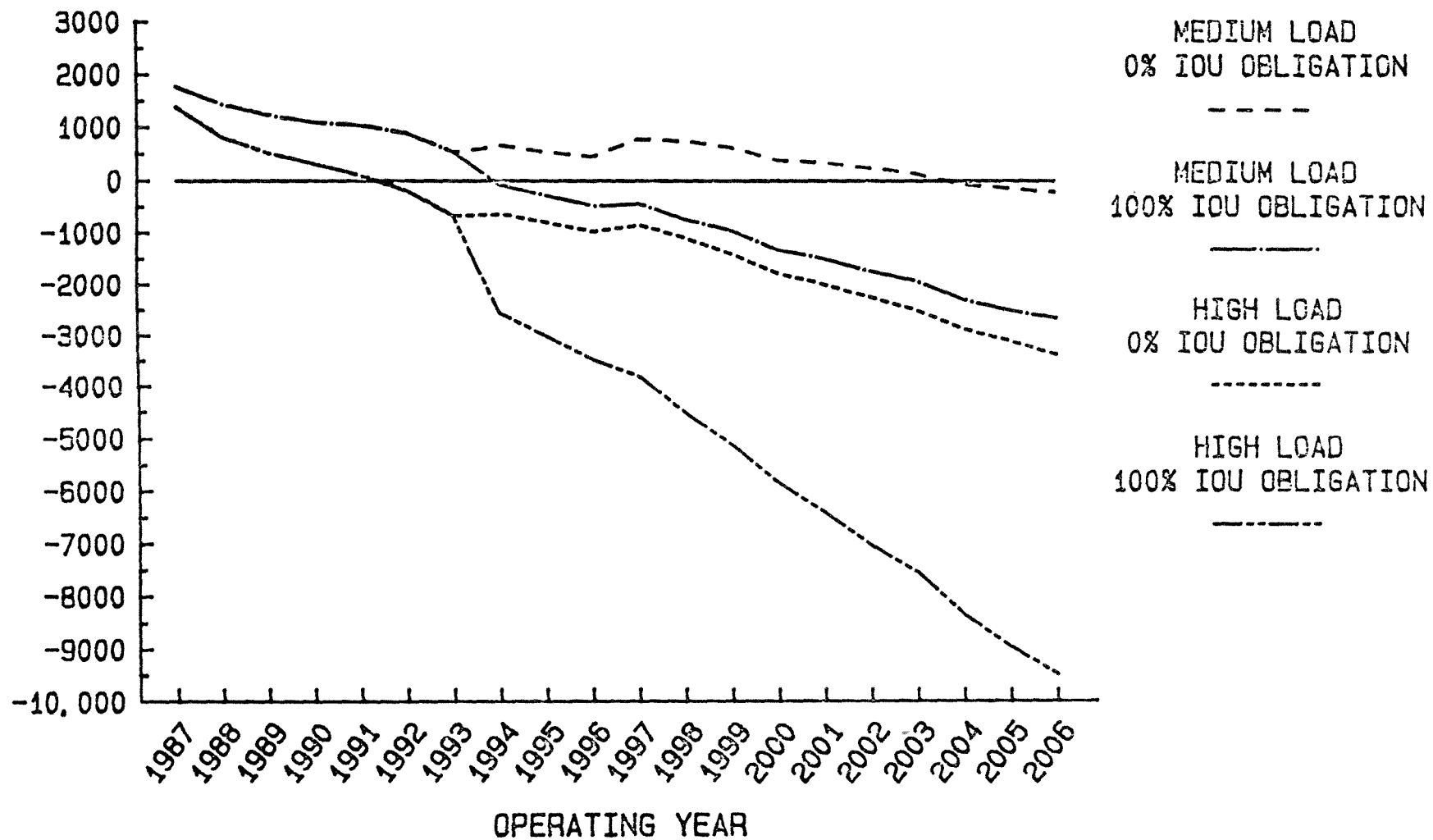


Figure 6
FEDERAL FIRM ENERGY SURPLUS/DEFICIT

AVERAGE MEGAWATTS





Department of Energy
Bonneville Power Administration
P.O. Box 3621
Portland, Oregon 97208-3621

OFFICE OF THE ADMINISTRATOR

In reply refer to: PKLC

SEP 17 1987

Mr. William Latham
General Manager
Sacramento Municipal Utility District
P.O. Box 15830
Sacramento, CA 95852-1830

Dear Mr. Latham:

On September 14, 1987, the Bonneville Power Administration (BPA) submitted a response to your recent Request for Proposals, describing a long term power transaction. As reflected in our response, BPA is prepared to provide power to the Sacramento Municipal Utility District (District) at a price below the District's alternative costs as indicated in the Request for Proposals.

BPA's proposal limited the amount of power available for sale to the amount of transmission capacity currently available to the District. BPA could sell the District 100 MW under the existing transmission access constraints, and would be willing to increase the amount of power sold assuming energization of the California/Oregon Transmission Project.

BPA would consider, however, increasing the amount of power available for sale to the District should additional transmission become available for the District's use. BPA is prepared to sell up to 725 average MW of firm power and 1350-MW of firm capacity to markets outside the Pacific Northwest region. The prices quoted in BPA's response are below the 42 mill-kWh rate quoted by the District as necessary to be competitive. As described in our response, BPA is also prepared to negotiate within the flexibility permitted under BPA's Long-Term Surplus Firm Rate Schedule SL-87 to meet the District's needs. It is our belief that BPA could provide enough power to make a substantial contribution towards meeting the District's resource needs, at least for the near future. This would be true whether or not Rancho Seco is brought back on line. If in the future BPA has insufficient surplus for the District's energy needs, BPA will have an ongoing capacity surplus which can be used to shape alternative resource capability for the District.

A sale of large amounts of power from BPA to the District would likely require the cooperation of the Pacific Gas and Electric Company (PG&E). For this

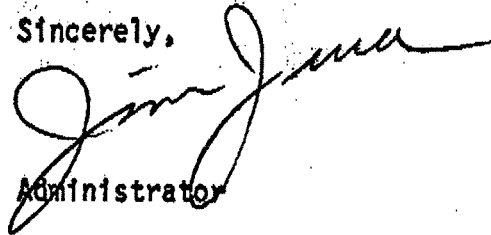


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reason we are also transmitting to PG&E a letter soliciting their interest in pursuing a joint venture. A copy of that letter is attached.

We look forward to your response.

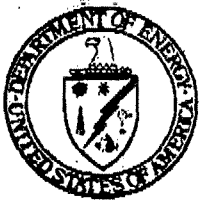
Sincerely,



Administrator

cc:

Mr. Richard A. Clark
District Board of Directors
Cliff Wilcox
Ed Smeloff
John Kehoe
Court Koehler
Ann Taylor



Department of Energy
Bonneville Power Administration
P.O. Box 3621
Portland, Oregon 97208-3621

OFFICE OF THE ADMINISTRATOR

In reply refer to: PKLC

SEP 17 1987

Mr. Richard A. Clarke
Chief Executive Officer
Pacific Gas and Electric Company
77 Beale Street
San Francisco, CA 94106

Dear Mr. Clarke:

On September 14, the Bonneville Power Administration (BPA) responded to the Sacramento Municipal Utility District's (District) Request for Proposals for resource purchases. BPA's proposal was limited to an amount of power equivalent to the District's existing contractual rights to transmission capacity to the Pacific Northwest. It appears, however, that the District's need for resources may exceed this amount. BPA is currently in a position to sell amounts of power in excess of that specified in its response to the District at prices we believe would be competitive with the District's alternatives. Consequently, transmission access may be a limiting factor in proceeding with economic arrangements.

Given that the District operates within the Pacific Gas and Electric Company (PG&E) load control area, it may be appropriate to consider a 3-party arrangement which would include PG&E, the District, and BPA. BPA is prepared to enter into discussions with PG&E in order to pursue a joint venture sale to the District. It is my belief that our systems may be well matched to provide the lowest cost resource to the District. Greater coordination of our systems is likely to benefit all our ratepayers.

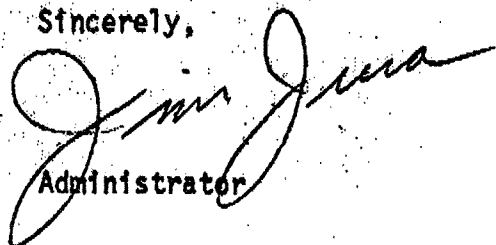
PG&E and BPA have often stated that it is in the interests of both the Pacific Northwest and California to achieve a balanced energy partnership which benefits both regions by promoting large amounts of energy transactions. BPA



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believes that a joint venture may be a good opportunity to further that partnership. I look forward to your response to our proposal.

Sincerely,

A handwritten signature in cursive script, appearing to read "Jim Jura", written over the word "Administrator".

Administrator

cc:

Mr. William Latham
District Board of Directors

Statement before the California Legislature
Assembly Committee on Utilities and Commerce
Hearings re: PG&E's Offer to Buy SMUD
6 October 1987

JAMES H. BUTZ
AIR PRODUCTS AND CHEMICALS, INC.

My name is James Butz. I am the Manager of Electricity Supply for Air Products and Chemicals, Inc. Air Products buys over \$6 million a year of electricity from SMUD. It is not an exaggeration to say that electricity is the lifeblood of Air Products. Using only electricity to drive large compressors, we liquify air and separate it into oxygen for hospitals and nitrogen for the semiconductor industry.

Our plants in Northern California are located in Santa Clara and Sacramento. It is not an accident that these facilities are both located on public power. Based on a detailed study of the costs for PG&E, Santa Clara and SMUD, we concluded that PG&E would be the highest cost utility.

For the last fifteen years this has been the case. Since 1974, SMUD has provided not only some of the lowest rates in California, but also some of the lowest in the country. This is due to SMUD's low cost resources: 20% government hydro, 30% owned hydro and 50% Rancho Seco. Rates were dramatically below PG&E even though Rancho Seco ran below the national average capacity factor (50% verses an average of 60%). If the plant had run as well as Duke's three plants of the same design, the savings would have been even greater. On the other hand, a significant portion of PG&E's electricity is produced from natural gas. Based on the high natural gas costs of the 1970's and the

California Commission's desire to subsidize both residential gas and electric consumers, PG&E's industrial electric rates were some of the highest in the country. Without the existence of SMUD or Santa Clara, we would have had no choice but to pay these higher rates.

Now natural gas is at its lowest price since the early 1970's. In the last three years, gas has dropped from \$6.00/MMBTU to \$1.80/MMBTU, which is roughly equivalent to a decrease of 6¢/KWH to 1.8¢/KWH. This drop has significantly reduced the cost of PG&E electricity. When this is combined with the increases at SMUD due to the Rancho Seco outage, the two utilities are close in costs for the first time in fifteen years. When the price of natural gas goes back up, PG&E rates will go back up with it.

In addition, PG&E has not yet obtained approval from the Commission to begin collecting for their own Diablo Canyon nuclear plant. Although this plant representing some of the most expensive electricity in the country will probably not be allowed in rates to the full extent, it will represent additional costs to PG&E ratepayers.

A merger between PG&E, the largest investor-owned utility in the U.S., and SMUD, the largest public power supplier in Northern California, would remove an alternative supplier from the market. A supplier who is not tied to the price of natural gas. This alternative is critical

to energy intensive companies like Air Products which need stable electricity prices over the long run.

A merger is not necessary to solve the Rancho Seco problem. It now appears that having Rancho Seco run by SMUD is only one of several alternatives to replace this needed resource. First, SMUD can continue to work with the NRC to satisfy the requirements for restart. Safety is obviously the first consideration in the operation or restart of any plant. Safety comes first at Air Products. We are not experts in nuclear safety; we rely on the Nuclear Regulatory Commission. The NRC has ordered the plant to stop running and we rely on their expertise to allow it to run again only if it is safe.

If SMUD's operation of the plant is not acceptable to the NRC, Duke has offered to operate the plant for SMUD. This proposal seems particularly attractive. Duke currently owns and operates three nuclear plants of the same design. These plants have the highest average capacity factors in the industry-over 70%. This compares to 50% for Rancho Seco before the current outage. PG&E's own consultant, Mr. Sawhill of McKinsey and Co., stated that Rancho Seco properly run would, in combination with SMUD's other resources, provide sufficient energy through the year 2000. The only additional resources needed would then be capacity which could be provided by pooling arrangements with other utilities. SMUD has rights to 200 MW on the existing

northwest intertie. Currently, SMUD has granted its use to PG&E until 1990. SMUD also has 400 MW on the new intertie scheduled for completion in the early 1990's.

A merger should be considered only as a last resort.

Twenty percent of SMUD's current energy is supplied under a long-term purchase contract within the U.S. Government in the form of the Western Area Power Authority (WAPA). This power is available to public agencies on a preference basis and would not be available to SMUD after a merger with PG&E. The power currently costs approximately 3¢/KWH and is not expected to escalate significantly.

In order to be beneficial, the merger must reduce the cost of electricity. This cannot be accomplished through arbitrary rate freezes which may subsidize some customers at the expense of others or simply postpone costs to a later date. Electric rates should be based on the cost of service. If the PG&E merger is truly beneficial, rates based on cost will show that and no arbitrary freeze will be needed. What good is a three-year rate freeze if rates double in year four?

Permanent closure of Rancho Seco may or may not be desirable. Yet PG&E proposes to close it unequivocally. Is this because it is the best alternative or is it because it provides a market for PG&E power?

PG&E is currently entering into contracts with

potential cogenerators to defer or cancel their projects. This power may be beneficial for SMUD. If purchased by SMUD, it would have to be delivered over PG&E lines. PG&E should be required to transmit cogenerated power or other power purchased by SMUD at rates commensurate with cost.

In Summary:

- A merger between PG&E and SMUD would be anti-competitive.
- A merger is not necessary to solve the "Rancho Seco problem".
- A merger should be considered only as a last resort and then only under the following caveats:
 - Rates based on the cost of service.
 - Economic analysis of Rancho Seco closure and other options before final action.
- PG&E should be required to wheel power to SMUD from other sources to further the competitive environment.

Thank you for the opportunity to present our views on a subject of vital interest to Air Products.

Statement before the California Legislature
Assembly Committee on Utilities and Commerce
Hearings re: PG&E's Offer To Buy SMUD
6 October 1987

JAMES H. BUTZ
AIR PRODUCTS AND CHEMICALS, INC.

Outline of Major Points

A merger between PG&E and SMUD is anti-competitive

- For the past 15 years SMUD's rates have been dramatically lower than PG&E's
- Rates are close now due to low natural gas prices and the Rancho Seco outage
- Not having SMUD would eliminate a needed alternative to PG&E. An alternative not tied to natural gas
- That alternative is critical to energy intensive industry like Air Products which need stable electric prices over the long term

A merger is not necessary to solve the Rancho Seco problem.

- It may be possible for SMUD to restart the plant
- If not, Duke Power has offered to operate the facility. Duke Power has three plants of the same design. Under Duke operation, these plants have the highest average capacity factor in the nuclear industry.
- Many other alternatives have been proposed to SMUD to provide long-term replacement power

A merger should only be considered as a last resort and then only under the following caveats:

- Rates based on the cost of service not arbitrary rate "freezes"
- An economic analysis of Rancho Seco restart and other alternatives prior to final action

Outline Continued

To enhance competition, PG&E should be required to transmit cogenerated or other purchased power to SMUD at rates commensurate with cost

- PG&E is signing contracts with retail customers to defer or cancel cogeneration projects
- This is power SMUD may need
- If PG&E does not need the power, PG&E should be required to transmit it to SMUD if requested.

COUNCIL OF SACRAMENTO SENIOR ORGANIZATIONS

1890 Geneva Place, Sacramento, CA 95825 Tel (916) 489-1751

BEFORE THE UTILITIES AND COMMERCE COMMITTEE, STATE ASSEMBLY
OCTOBER 6, 1987

My name is Edmund Lewis, Immediate Past President and Chairman of the Utility Committee, Council of Sacramento Senior Organizations. The Council is made up of representatives of almost all of the major senior organizations in Sacramento County.

We would like to make a brief prepared statement, and then respond to any questions you may have.

First, current law relating to SMUD, a publicly owned utility, is not working satisfactorily. We are referring specifically to Sections 14403, 14403.3 and 14403.5 of the Public Utilities Code--relating to rate hearings. The process that the SMUD Board has devised under the law has proven to be devisive and frustrating. In all fairness the Board is attempting, after considerable nudging, to improve the process. It may need, however, some help from this Committee.

While we do not want the highly formalized procedures of the PUC, we need a system that will be responsive to ratepayer testimony and requests. The General Manager's report, required by law, needs to be prepared in easy-to-understand language and format. Workshops about the report should be held in each Ward of the District. Rules and regulations about the rate hearing process that provide fair and equal treatment should be adopted and be available to the public at each meeting. The rate hearing process should be

lengthened to include at least two meetings with testimony--permitting the staff to "hear" and react to the public input. There are many more details that can be provided if this committee wishes to pursue the matter. Suffice it to say, we believe the law should be amended.

We would also recommend that the Board members receive training. The lack of trust and teamwork among the Board members and with staff is apparent. Unethical board practices must stop. Compliance with the Brown Act should be enforced--with penalties if necessary. SMUD is a public utility and the public's business should be conducted in public.

* * * * *

Next we would direct your attention to Attachments "A" and "B" at the end of this testimony. Please note that we are discussing the average monthly electricity bill rates for the residential customer who heats with gas. These rates went into effect on October 1, 1987. SMUD rates are higher than PG&E for the first 750 KWH! And only in the residential class does SMUD have higher rates. The net result is that low income, low-user seniors and the poor are currently paying more in an arcane and unfair SMUD rate structure. Although the new rate structure provides a "modified Baseline" rate for the first time, it is a long way from being satisfactory.

Then along comes PG&E with its offer to take over SMUD and freeze rates at current levels. Preposterous!!!

According to PG&E figures, 53 percent of the people in the SMUD residential class would continue with the higher SMUD rates "for several years" if a PG&E-SMUD consolidation took place. Needless to say, PG&E did not consider the negative political consequences of

of such a move. This matter was called to the attention of top PG&E executives prior to their appearance at the SMUD Board meeting on October 1. Unfortunately, they did not see fit to retract or modify the PG&E freeze statement. While seniors are not against growth per se, they do not want to pay excessively for the rapidly expanding Sacramento market.

Most seniors are in the residential class using 750 kilowatts or less a month. They are angry!

The bottom line, of course, is....rates. Neither SMUD nor PG&E are giving sufficient attention to the poor and those on fixed income at this time. The current SMUD rate structure and the promised PG&E rate freeze prove that this is true.

* * * * *

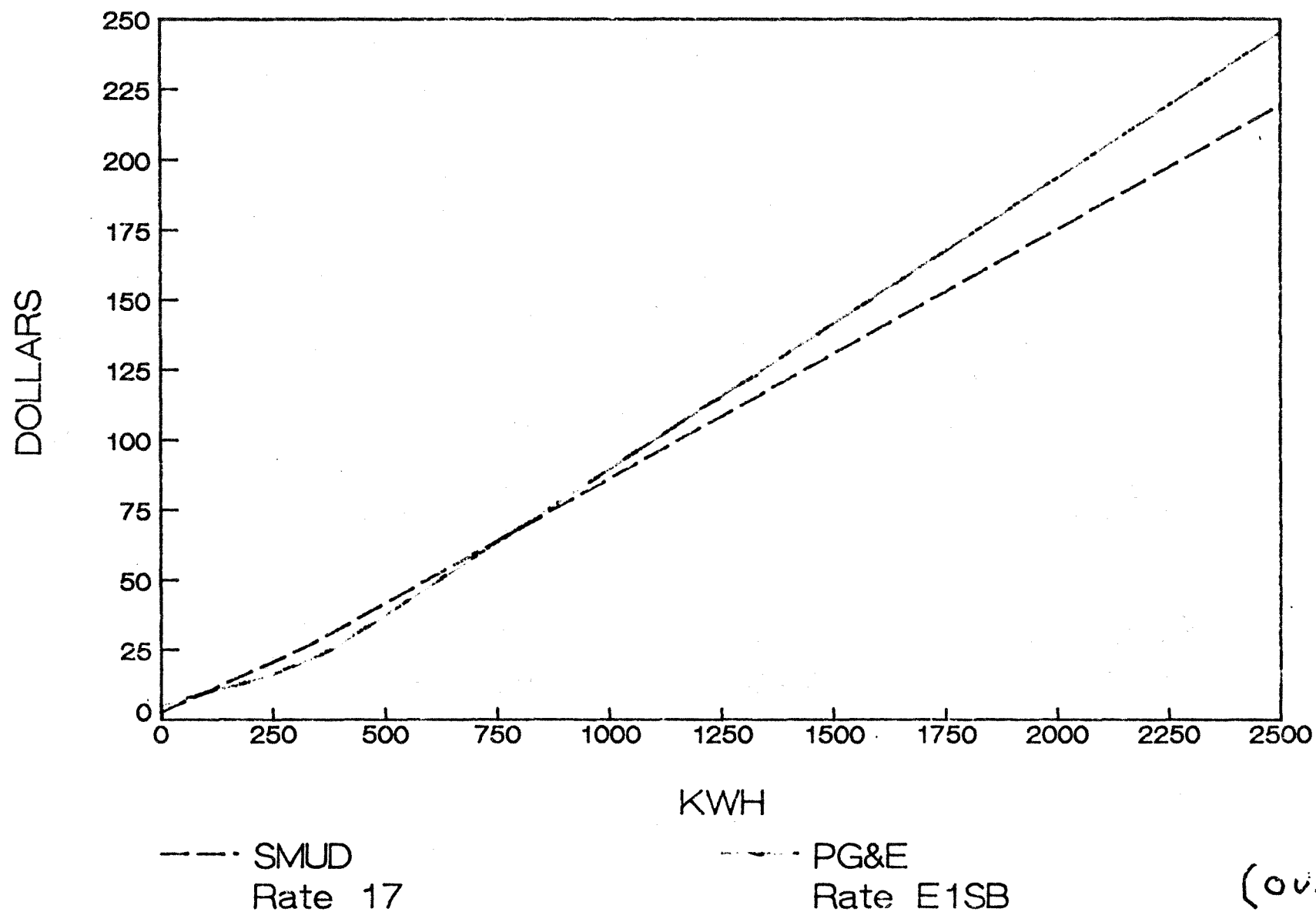
Finally, let's discuss the total utility picture in Sacramento County. This includes, but is not limited to public, private and city utilities such as gas, electricity, telephone, water, sewer, garbage disposal, transportation, etc. Senior citizens, on fixed income are finding the continuous utility rate increases and utility taxes intolerable. As you know, SMUD'S rates have increased 84 percent. On top of this Regional Sewer rates are up 38 percent this year, and the Sacramento City utility tax is the highest in the state at 8 percent. Yet seniors received a 1.3 percent COLA from Social Security this year. The problem is exacerbated when no one in government seems to know (or really care) what happens when each government entity and each utility acts in its own self interest, and raises rates/taxes a seemingly small amount. The cumulative effect is as devastating as runaway inflation for those on fixed income.

With Proposition 13 and the Gann limit in force, the total spectrum of utility rates and utility taxes have increased markedly. Senior citizens and the poor need utility rate/tax relief. We hereby request this committee to:

- 1 - Gather and analyze utility rate and utility tax information, showing trends, for all utilities; by county and each city within the county. With this information the Committee will be able to make better policy decisions, and determine what is the cumulative effect on the citizens who must pay the bills.
- 2 - Provide equitable utility taxes. The present utility tax is being levied in about 40 cities--and is not equitable. We suggest you hold hearings and take affirmative action on Assembly Constitutional Amendment 4. We support the ACA.

Thank you.

RESIDENTIAL - GAS SPACE HEATING AVERAGE MONTHLY COMPARISON BILLS



(OVER)

RESIDENTIAL RATES
Effective 10/1/87

SUMMER

<u>KWH</u>	<u>SMUD</u> <u>RATE 17</u>	<u>PG&E</u> <u>EISB</u>	<u>KWH</u>	<u>SMUD</u> <u>RATE 14</u>	<u>PG&E</u> <u>EISH</u>
250	\$ 20.70	\$ 16.16	250	\$ 21.60	\$ 16.16
500	41.49	36.53	500	41.24	32.33
750	63.73	62.52	750	63.47	54.50
1,000	85.96	88.51	1,000	85.71	80.49
1,500	130.43	140.49	1,500	130.18	132.47
2,000	174.90	192.47	2,000	174.65	184.45
2,500	219.37	244.45	2,500	219.12	236.43

WINTER

250	\$ 20.67	\$ 16.16	250	\$ 17.27	\$ 16.16
500	41.86	38.18	500	30.98	32.33
750	64.06	64.17	750	45.38	48.49
1,000	86.26	90.16	1,000	62.28	64.65
1,500	130.65	142.14	1,500	96.07	115.96
2,000	175.05	194.12	2,000	129.87	167.94
2,500	219.44	246.10	2,500	163.66	219.92

ANNUAL MONTHLY AVERAGE

250	\$ 20.68	\$ 16.16	250	\$ 19.43	\$ 16.16
500	41.68	37.36	500	36.11	32.33
750	63.89	63.35	750	54.43	51.49
1,000	86.11	89.34	1,000	73.99	72.57
1,500	130.54	141.32	1,500	113.13	124.22
2,000	174.97	193.30	2,000	152.26	176.20
2,500	219.41	245.28	2,500	191.39	228.18

(OVER)